Canfor Corporation Annual Report 2002

Morning. Midday. Midnight. There wasn't a moment throughout the year that the Canfor team wasn't working hard, rolling up their sleeves, and doing their part to get the job done. Because when you're a leader, you focus on the now. Now's the time to work harder. Now's the time to make the tough decisions. Now's the time to stay focused on our strategy. **Now's the time.**

View Canfor's Annual Report On-Line

A printable version of Canfor's Annual Report is available on-line. To access the PDF file, please go to www.canfor.com and click on "Investors".

To reduce annual report production costs and avoid duplication, we are in the process of updating our corporate mailing list. If you still prefer to receive a printed Canfor Annual Report rather than viewing the publication on-line, please indicate below and confirm the number of copies you wish to receive.

If you are currently a shareholder, you should automatically receive an Annual Report and need not be included on this mailing list. Check with your financial advisor or institution to confirm.

Your cooperation in assisting us to update our mailing list is appreciated. Please reply by April 30, 2003. If you have any questions, please contact us by phone at 604-661-5305, fax 604-661-5219 or e-mail: info@canfor.ca.

Do you wish to continue to receive Canfor's Annual Report in the mail:

Yes: ☐ No: ☐

If yes, indicate number of copies required:

____

Indicate correct name and address in the space provided:

Name: ____________________

Address: ____________________

____

____

____

Corporate Profile

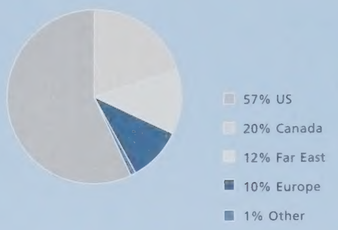
Canfor Corporation is a leading Canadian integrated forest products company based in Vancouver, B.C. The company employs approximately 6,290 people - 5,600 directly, and 690 through affiliated companies.

Canfor has extensive woodlands operations and manufacturing facilities in British Columbia and Alberta, and a lumber re-manufacturing plant in Washington State. The company is a major producer and supplier of lumber and bleached kraft pulp. It also produces semi-bleached and unbleached kraft pulp, bleached and unbleached kraft paper, plywood, remanufactured lumber products, hardboard paneling and a range of specialized wood products, including baled fibre and fibremat. Howe Sound Pulp and Paper Limited Partnership, owned equally by Canfor and Oji Paper Co., Ltd., produces bleached kraft pulp and newsprint.

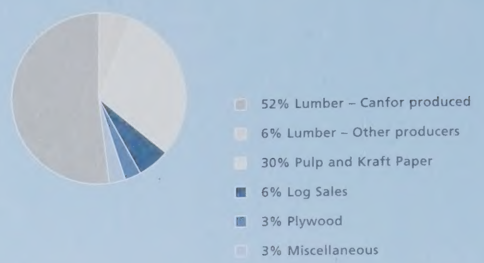
Canfor's products are sold in global markets. The company has marketing offices in Canada, Europe and Japan.

Canfor Corporation is listed on the Toronto Exchange and trades under the symbol 'CFP'. The main operating company is Canadian Forest Products Ltd., from which the name Canfor is derived.

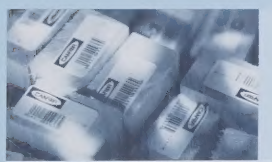
Net sales by market



Net sales mix by product line



Canfor Business Units

		PRODUCTS	PRIMARY MARKETS	2002 HIGHLIGHTS
	Wood Products	> Softwood Lumber and Plywood > Hardboard Products > Refined Fibre > Fibremat	> House construction and home repairs and renovations > Wall panels for home construction and renovations > Erosion control > Car components (door panels, dashboards)	> Achieved record lumber production of 3 billion board feet > Reduced conversion costs by 7% > Obtained largest SFI certification in Canada
	Pulp Products	> Premium Pulp	> Raw material for paper manufacturing (printing, fine, and tissue papers)	> Achieved record pulp production of one million tonnes > Reduced costs by 9% > Earned "Highest Rated Paper Supplier"
	Pulp and Specialty Kraft Paper	> Specialty Kraft Paper > Specialty Pulp	> High performance packaging papers and specialty papers > Raw material for paper manufacturing (base and electrical application papers)	> Improved tonnes of paper to customer order by 44% from 1st quarter to 4th quarter > Reduced costs by 4%
	Coastal Operations	> Primarily hemlock, cypress, Douglas Fir, and cedar logs	> Coastal pulp mills and sawmills	> Improved EBITDA by 9% to 11% > Realized 11% improvement in sale prices > Reduced costs by 3%

Please see page 73 for a listing of production and capacity figures.

		2002	2001
Sales and income (millions of dollars)	Net sales	$ 2,112.3	$ 1,985.7
	Operating income	55.1	62.5
	Net income	11.5	26.4
Cash flow (millions of dollars)	Cash flow from operations	$ 144.4	$ 118.8
Per common share (dollars)	Net income	$ 0.07	$ 0.27
	Net income – diluted	0.07	0.27
	Dividends	0.26	0.26
	Book Value	10.27	10.35
	Share price		
	High	11.63	12.60
	Low	6.95	8.05
	Close - December 31	8.85	9.80
	Common shares outstanding – weighted average	81,156,010	81,088,847
Financial position (millions of dollars)	Working capital	$ 273.2	$ 342.3
	Total assets	2,328.0	2,378.8
	Long-term liabilities	727.3	833.1
	Common shareholders' equity	953.9	960.5
	Total capitalization	1,931.4	2,044.6
Additional information (1)	Return on capital employed	2.7%	3.5%
	Return on common shareholders' equity	1.2%	2.8%
	Ratio of current assets to current liabilities	1.7:1	2.0:1
	Ratio of net debt to common shareholders' equity	41:59	43:57
	EBITDA (millions of dollars)	$ 170.2	$ 168.5
	EBITDA margin	8%	8%
	Capital expenditures (millions of dollars)	$ 68.5	$ 54.7

(1) See Definitions of Selected Financial Terms on page 46.

Dear fellow shareholder,

Sometimes it's hard to know whether to despair, celebrate, or just get used to it, but the 2001 message to shareholders could have served well if written in reference to 2002. With lumber and pulp accounting for 75% of Canfor's revenues, we endured the lowest prices in over a decade for both major product lines. Add the punishing effects of 25% duties on lumber sold into the US market, with Canfor carrying the largest share of the burden of any Canadian forest products company, and you have the makings of a very bad year.

And, it was a very tough year, yet we have more cause for celebration than despair. Hit with the worst possible combination of market circumstances, we were able to stand our ground against the attack from the American protectionist juggernaut.

An $11 million profit in 2002 may not be exciting but it was a remarkable achievement by the people of Canfor. They reduced costs aggressively, they set production and productivity records, they kept Canfor at the forefront of the industry in terms of safety and environmental performance, and they held our market share in the face of extreme adversity.

Late in 2002, a far-reaching plan to further improve our permanent operating income base by at least $150 million was developed and is now being implemented. Costs are being reduced in all areas with the most dramatic changes occurring in operations. Mills are being rationalized so that we will have fewer mills operating on a virtually continuous basis, employing skilled personnel, the most current technology and modern process controls. The recently announced closure of one sawmill near Prince George and one in Taylor, B.C. were part of this plan. Decisions to complete the sawmill optimization program in the Prince George Region, Houston, as well as the Peace Region of B.C. and Alberta are scheduled to be taken before the end of July. A key factor in this restructuring is the evolving fibre situation in our operating areas.

12:17 pm

David L. Emerson, President and Chief Executive Officer

Our commitment is to build a strong and healthy company that delivers exceptional value to shareholders, a safe and rewarding workplace for our people and economic stability for the many communities that depend on us.

Peter J.G. Bentley, Chairman

Similar cost reducing, productivity enhancing and margin improving actions are being implemented in the Pulp and Paper Group.

Protectionistic trade actions by the United States have disrupted and hurt the Canadian softwood lumber industry for many years. The new extremes the protectionists have gone to in the current dispute are unprecedented and may well be the seeds that destroy their own cause.

In the face of both anti-dumping duties and countervailing duties, Canadian companies are fighting back. They are reducing costs with a vengeance; they are pursuing all legal remedies; and they are conducting an effective media campaign to inform Congress and the millions of people who depend on free and open trade for their jobs and for the health of thousands of businesses in the US.

Perhaps most important, governments in Canada, led by British Columbia are calling the great protectionist bluff. Our governments are moving to reform forest policies, timber pricing and regulation to make them more market based, more transparent and more impregnable to attack by self-serving trade actions launched against the Canadian industry.

We are at a critical crossroad in the history of softwood lumber trade with the US. We are at the point where the underpinnings of protectionist allegations are about to be destroyed by policy changes in Canada. While the territory is uncharted and there is considerable uncertainty, we are closer to the end of this saga than to the beginning. Whether through litigation - at NAFTA and

WTO, or through a negotiated solution, there is little doubt that we will see a trend to freer trade and we will see the forest products industry in North America emerge stronger, more integrated and more globally competitive as a result.

Canfor is building a foundation for success in this emerging new environment. We have already separated our woodlands and fibre management from manufacturing. The mandate of this group is to optimize the value of timber to Canfor as the changeover to market-based timber management systems takes hold.

With our cost base being reduced on an urgent and focused basis, we are prepared to persevere in our battle against American protectionism, and we will be among the world's most efficient managers of softwood lumber supply chains. Long-term prospects for wood products markets are good and our presence in a variety of global markets continues to strengthen.

Add to this the improvement we are seeing in pulp and paper markets and we should see significant improvement in Canfor's prospects over the next year or two.

We continue to take significant steps to strengthen our balance sheet, while improving efficiency and growing our core wood products business. And, we are proud of the fact that we have maintained our dividend payments, despite adverse industry conditions.

Our commitment is to build a strong and healthy company that delivers exceptional value to shareholders, a safe and rewarding workplace for our people and economic stability for the many communities that depend on us.

Our thanks to our employees, our Board of Directors and our shareholders as we emerge from the unprecedented adversity of the past few years and begin again to capitalize on opportunities for significantly improved financial returns.

Peter Bentley

Peter J.G. Bentley
Chairman

David Emerson

David L. Emerson
President and Chief Executive Officer


HARD HATS &
HEARING PROTECTION
REQUIRED

12:06 am

Mike Behm, Spareman, Rustad Sawmill

Leaving the mill after finishing his afternoon planer shift, as the graveyard shift begins. Canfor is adding third shifts and maximizing production at its sawmills to lower costs and achieve top quartile performance.

Maximizing capital utilization and efficiency

3:09 am

Wayne Guthrie, GM North American Sales and Marketing - Canfor's Wood Products Group

Reviewing lumber production figures en route to a customer meeting. Delivering a quality product, coupled with excellent customer service, has helped increase Canfor's North American lumber market share and secure new customers around the globe.

Going out of our way to understand customer needs

8:51 pm

David L. Emerson, President and Chief Executive Officer
Charles Reid, Group Vice President, Finance and CFO

Reviewing progress on Canfor's company-wide Cost Reduction/Margin Improvement Program. Announced in the fall of 2002, the Program will achieve $150 million in structural improvements on an annualized basis by the fourth quarter of 2003.

Increasing profitability starts at the top

5:22 am

Judy Vasily, Planning Forester

Preparing to leave for a surveillance audit of Canfor's Sustainable Forest Management (SFM) certification at Tree Farm Licence 30 in Prince George. Canfor has expanded its SFM certification which now encompasses 63% of its tenure area and 73% of its harvest volume.

Managing the environment around the clock


24—11

10:38 pm

Steve Bates, Electrician, Northwood Pulp Mill

Scanning pulp mill equipment with state-of-the-art infrared cameras to detect potential maintenance issues is part of Canfor's Predictive Maintenance Program. This Program will result in maintenance shutdown reliability savings of $14 million per year.

Minimizing downtime through preventative maintenance


Certification
0
02
Governed by Sustainable Forestry Management Certification (CSA and SF

Air Quality

Canfor is fully engaged in Air Quality Management in the communities where we operate. With a long history of burner closures, emission control upgrades and contributing to the cost of ambient monitoring equipment, staff have most recently stepped up to serve on newly formed committees in Prince George and in the Bulkley Valley. Research is pointing to a need to address area sources like road dust, vehicle emissions and wood stoves and Canfor is looking to participate wherever efficient, effective actions are identified.

Thermal Oil Systems Task Force

A task force was struck in 2002 to develop a Canfor Engineering Standard for Thermal Oil Systems. Several Canfor sawmills operate these systems that burn wood residue to heat oil for transfer to lumber dry kilns and buildings. This Standard will include environmental specifications for maintenance, operation, upgrades and design of new systems. These units represent a value-added use for the residue while offsetting the need for fossil fuels. Completion of the Standard is planned for the second quarter 2003.

Thermal oil system operators participated in an information exchange/training session in the Fall of 2002.

Value-added Uses for Wood Residue

Canfor is actively seeking opportunities to create value from the surplus wood residues generated at our sawmill operations. A $1.7 million project completed in November 2002 at Northwood Pulp has improved the mill boiler controls and resulted in substantially increased wood residue incineration in the boilers. In addition to more efficiently burning wood residue that previously would have been burned in inefficient beehive burners, this project has reduced natural gas purchases and improved NW Pulp's bottom line. Canfor is also actively pursuing electricity cogeneration projects in Grande Prairie Alberta and Houston British Columbia, which will generate electricity from renewable sawmill wood residues, allow for the closure of beehive and silo burners, and reduce Canfor's particulate and greenhouse gas emissions.

Potable Water Program

An ambitious 18 month program to assess and protect Canfor's potable water systems concluded in late 2002. Trained Water System Managers are now in charge of the 43 Canfor-owned systems as well as a host of contractor facilities. A Canfor Water Management Standard outlines regulatory requirements, roles and responsibilities and the water sampling program. A module to house information on the complex and varied systems was developed by Genus™. This high-tech system also reminds operators when samples are due and provides an early warning to water quality issues identified at the lab. All Canfor systems have been assessed by L&M Engineering Limited of Prince George and work has already begun on recommendations for upgrades. Ministry of Health Planning staff have been supportive throughout this process.

FORESTRY

Compliance Report

In anticipation of the British Columbia government's transition to results-based forest practices legislation, Canfor continued to improve processes around the internal monitoring and reporting of our forestry practices. As a result, during 2002, 69% of all non-compliance incidents related to Canfor's forestry activities investigated by government agencies were originally detected and reported by Canfor staff. In all cases, Canfor promptly took necessary actions to mitigate any environmental consequences and correct conditions that may have led to the incident. A total of 96 non-compliance incidents occurred on company tenures during 2002, 12% fewer than in 2001.

Figure 1 – Non-compliance incidents by volume of timber harvested

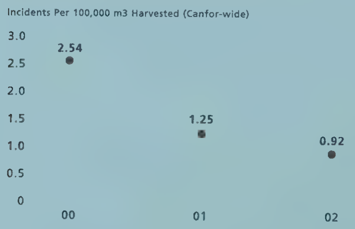


Figure 1 indicates the trend in total number of non-compliance incidents on Canfor operations per 100,000 cubic metres of timber harvested for the period 2000 to 2002.

British Columbia government agencies assessed eleven administrative penalties under the *Forest Practices Code Act* to Canfor during 2002, totalling $10,645. None of the assessments involved environmental damage. Six of the incidents for which penalties were assessed occurred prior to 2002. Several other determinations of non-compliance were declared by government agencies, but no monetary penalties were assessed, in part because of the minor nature of the infractions and Canfor's prompt mitigation and corrective action. The company also received two official written warnings for non-compliance under the British Columbia *Pesticide Control Act*, following audits of herbicide application records. These incidents were related to administrative procedures and did not result in any environmental consequences.

No administrative penalties were assessed to Canfor by Alberta government agencies in 2002, although Canfor reported several incidents involving small quantities of herbicide application outside of prescribed treatment boundaries.

Canfor forestry operations reported twelve spills to government agencies in 2002. Eleven of the spills occurred in British Columbia and one occurred in Alberta. All spills were minor in nature and were appropriately managed. Six of the spills were the result of equipment failure, four followed motor vehicle accidents, one resulted from an act of vandalism and one resulted from the sinking of a boom boat. Only the boom boat incident resulted in the release of controlled products to water bodies. In that case approximately eight litres of diesel was released, but was promptly contained and recovered. A fire started due to spontaneous combustion in a large debris pile at a dry land sort.

Certification

Although the majority of Canada's forest industry is now moving toward environmental certification of its operations, Canfor's reputation as a leader in the eco-certification of forestland and forest products continued to grow in 2002.

All Canfor forest operations in the Prince George and Quesnel Timber Supply Areas and Tree Farm Licence (TFL) 30 were certified to the Sustainable Forestry Initiative® (SFI℠) Standard of sustainable forestry during the year. This represented the first SFI℠ certification for Canfor and the largest, by area, in Canada. With the addition of the SFI℠ certified area to the suite of tenures already certified to the Canadian Standards Association (CSA) Sustainable Forest Management (SFM) Standard, Canfor now has more than half of its tenure area governed by certified SFM plans. This includes 73% of the company's annual harvest volume. Meanwhile, the Environmental Management System (EMS) for forestry operations underwent a comprehensive third party assessment in 2002 and the system has been recommended for re-registration under the ISO 14001 standard. The scope of Canfor's forestry EMS includes all Canfor forestry tenures.

SFI℠ and CSA registration audits at the Fort St. John and Houston operations are planned for 2003. If successful, the registrations will increase Canfor's managed forestland certified to an SFM standard by an additional 4.9 million hectares.

Performance Versus Objectives in 2002

Canfor established seven environmental objectives for 2002, aimed at achieving continuous improvement in our forestry operations. Specific and measurable targets were set for each of the objectives at either the corporate or regional level.

Objective: Conduct activities consistent with project plans.

Figure 2 – Trespass or environmental damage determinations

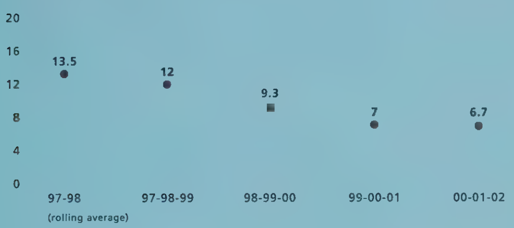


Figure 2 indicates the trend in trespass or environmental damage determinations for the period 1997 to 2002. These incidents are usually caused by a failure to follow project plans. All determinations during 2002 in this category were related to minor boundary trespasses that occurred during timber harvesting operations.

Performance: Riparian resources, including those habitats associated with streams and lakes, are an ecologically significant component of forests. Canfor takes special care when conducting activities adjacent to riparian resources and we established a number of targets to improve our performance in these areas.

Figure 3 – Non-compliance incidents related to riparian resources

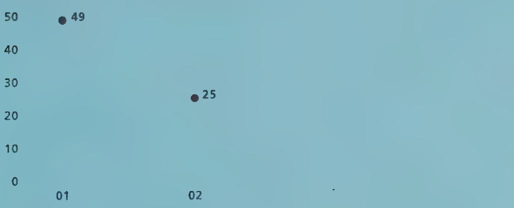


Figure 3 illustrates one aspect of the company's performance related to riparian management; a reduction in the number of non-compliance incidents related to riparian resources in 2002 compared to the previous year.

Objective: Prevent spills and leaks of harmful products.

Performance: Canfor contractor crews, and company crews at coastal operations continued to demonstrate a high level of awareness of emergency preparedness and response procedures. Although the corporate target of zero reportable spills on forestry operations was not achieved in 2002, the response to spills that occurred during the year was prompt and effective.

Objective: Minimize the impact on forest resources resulting from uncontrolled fire.

Performance: Uncontrolled fire is recognized as one of the highest risk environmental aspects affecting forestry operations. Consequently, Canfor has developed numerous operational controls to manage our activities in such a way as to prevent forest fires and to respond promptly when required with appropriate fire fighting resources. Targets associated with this objective were satisfactorily met at all company operations during the year.

Objective: Balance environmental, economic and social objectives in forest-level planning.

Performance: This objective was addressed through targets contained in SFM plans that are in place at all Canfor forest regions. Reporting on the status of these targets is communicated through SFM annual reports, and results are verified through third party audits as a component of SFM certification.

Objective: Incorporate management strategies into operational plans to address significant aspects.

Performance: The process for risk ranking of Canfor's environmental aspects for forestry operations was completely revised during 2002, in order to improve the transition from strategic level SFM plans to operational phases when on-the-ground activities are carried out. Significant progress was made during the year to implement monitoring and measurement processes, designed to verify that plans are achieving intended results. This included the implementation of several new or enhanced information management modules developed by *Genus RMT*.

Objective: Improve public and employee confidence in our environmental practices.

Performance: Several targets were set and achieved at each Canfor forest region to improve communication with the public. Examples include the ongoing participation of public advisory groups or committees in the SFM planning process and creation of opportunities for the involvement of aboriginal people in forestry planning activities.

Objective: Minimize impacts to other resources due to misapplication of chemicals.

Performance: The application of chemicals on Canfor forest tenures is primarily limited to the use of herbicide for vegetation management on some reforested areas. As these activities are strictly governed by legislation, all targets reflect the necessity that herbicide application be in conformance with legal requirements. In 2002, herbicide program performance targets were substantially met at all operations. Several minor incidents occurred where a small amount of herbicide was applied outside proposed treatment boundaries. No environmental damage occurred as a result of these incidents and all were promptly reported to government agencies.

Objectives and Targets for 2003

2003 environment objectives for forestry have been expanded to capture the social and economic aspects of our operations and enable us to apply sustainable forest management principles at all our operating areas. Specific targets for each objective have been set at all Canfor forest regions.

(Biological Diversity) Conserve biological diversity by maintaining ecosystem, species and genetic diversity at a landscape level.

(Ecosystem Resilience and Productivity) Conserve ecosystem processes by maintaining healthy, resilient and productive forest ecosystems.

(Global Ecological Cycles) Maintain forest conditions and management activities that contribute to the health of global ecological cycles.

(Pollution) Minimize impacts to other resources by preventing spills and leaks of harmful products and the misapplication of chemicals.

(Balanced Use of Forests) Plan and conduct activities to provide a balanced mix of timber and non-timber benefits.

(Human Health and Safety) Operate in a manner that protects human health and safety.

(Community Involvement) Create opportunities for interested parties to have input into forest planning activities.

(Aboriginal Interests) Incorporate aboriginal interests into strategic and operational planning.

(Accountability) Communicate our sustainable forest management performance to interested parties.

(Timber Supply) Manage the forest to produce a long term supply of affordable timber.

(Fair Return on Investment) Manage the forest to provide a fair return on investment.

(Fair Distribution of Benefits and Costs from the Forest) Manage the forest to provide economic benefits to local communities, shareholders and government.

(Mutually Beneficial Business Relationships with Aboriginal People) Pursue business partnerships and cooperative working arrangements with aboriginal people.

MANUFACTURING

Compliance Report

Canfor is committed to transparency in our environmental reporting and includes compliance reporting as part of this process. The following is an inventory of compliance for Canfor's manufacturing operations, including Howe Sound Pulp and Paper Limited Partnership (HSLP).

In 2002, Canfor and HSLP had the following non-compliance situations (reported in accordance with government non-compliance reporting criteria):

Air

One beehive burner regularly operated below approval temperature due to lack of fuel on the afternoon shift. Improvements have been made to the burner structure and operating controls are being optimized to ensure compliance. A written warning was received for one burner failing to meet temperature compliance for several days in the first quarter and two burners failed to meet compliance temperature for four and five days in the first four months of 2002. Two written warnings were issued for burner noncompliance incidents that occurred in 2001. At pulp mill operations, a particulate test on a smelt dissolving tank stack and a lime kiln stack failed to meet Permit limit. Reduced scrubber efficiency at a chemical plant caused the plant to exceed the Permitted limit for vented chlorine emissions for a period of one day.

Effluent

On two occasions at a chemical plant, small quantities of process liquor were released to a tank which discharges to the river. Preventive measures have been implemented.

Landfill

N/A

Spills

Canfor and HSLP manufacturing operations had 17 reportable spills in 2002. All have been contained, cleaned up and preventive actions taken. Spills included: two spills

of log conditioning chest water to ground; two low volume spills of black liquor to ground; six spills of pulpmill process effluent/clarifier sludge/ filtrate to ground; three spills of hydraulic oil to ground; one spill each of caustic soda, reactor spent acid and crude tall oil to ground; and one spill of chlorine dioxide to ground.

Performance versus Objectives in 2002

Wood Residue Utilization

Objective: We will continue to pursue opportunities to substantially increase utilization of our sawmill wood residues and thereby achieve our beehive burner phase-out commitments.

Performance: Canfor implemented the Northwood Pulp Mill boiler controls project in 2002 and is actively pursuing two significant biomass electricity cogeneration projects (Grande Prairie and Houston) which will substantially increase our wood residue utilization.

Greenhouse Gases (GHG)

Objective: We will implement our greenhouse gas strategy.

Performance: Canfor's greenhouse gas emissions for 2001 (the most recent reporting year under Canada's Voluntary Climate Registry Program) were 8-9% below 1990 levels and below Canada's Kyoto commitment of 6% below 1990 levels by 2010 – 2012. We are projecting that with projects underway or contemplated, Canfor's GHG emissions will be 10 – 15% below 1990 levels by 2005.

Audits

Objective: We will carry out corporate environmental audits of one pulp mill, four sawmill operations, two remanufacturing plants, and a chemical plant.

Performance: Internal audits were carried out as planned and, in addition, an internal pre-registration audit was conducted at the Rustad Sawmill in preparation for the ISO 14001 registration audit.

EMS

Objective: Management reviews will be completed and environmental objectives and targets established at all of our sawmill operations.

Performance: Management reviews have been completed and environmental objectives and targets have been set at all sawmills as well as two remanufacturing plants, one plywood plant and one wood treating plant. In addition, in December 2002, the Rustad Sawmill EMS received registration to the ISO 14001 Standard for environmental management.

Potable Water Program

Objective: We will develop and implement a Canfor Water Management Standard which includes operator training, water quality testing, an emergency response plan and a data management system.

Performance: Water System Managers have been trained. A water quality testing program has been implemented and the data management system is functioning. The Canfor Water Management Standard, with an Emergency Response Plan template, has been approved by Senior Management. In addition, all Canfor-owned water supply systems have been assessed by a qualified engineering firm.

Objectives and Targets for 2003

The following are corporate level objectives and targets for 2003.

(Wood Residue Utilization) We will continue to actively pursue opportunities to substantially increase utilization of our sawmill wood residues such as electricity cogeneration at our pulp mills and sawmills and wood residue fueled energy systems at our sawmills.

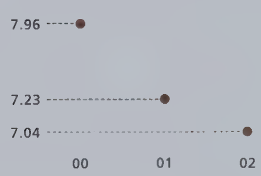
(Greenhouse Gases) Through projects which increase utilization of our sawmill wood residues and offset electricity and natural gas purchases, we will continue to reduce our greenhouse gas emission profile.

(Audits) We will carry out corporate environmental audits of three pulp mills, four sawmill operations, one panel board plant, and a wood treating plant.

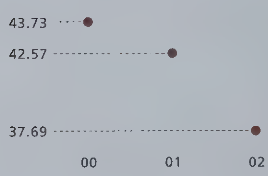
(Wood Products EMS Enhancement) We will enhance Wood Products EMS including training needs assessments relative to significant aspects, emergency/spill response training and EMS documentation.

(Thermal Oil Systems) We will complete and implement a Canfor Engineering Standard for Thermal Oil Systems that ensures environmental aspects relating to these systems are considered and managed.

Medical Aid Frequency



First Aid Frequency



Realigning our employees to meet strategic business objectives:

- Third shifts in place at Polar and Isle Pierre operations
- Third shifts introduced at Fort St. James and Rustad sawmills
- Third shift successfully negotiated for the Fort St. John facility

Employees are an integral part of the company contributing to the overall success of Canfor. It is important that Canfor's employees be aligned to meet strategic business objectives. To this end, Canfor paid particular attention to the communication of these objectives to both the union and salaried employees within the company. This process was designed to ensure that everyone working within the company understood Canfor's strategic direction in the context of the market realities and assisted greatly in the company's transformation.

An extension of aligning the employees with the strategic objectives of the company resulted in some innovative activity at both the Pulp and Paper and Wood Products operations. Late in the year, Canfor commenced with the early negotiation of contracts with its pulp unions with the objective of providing a horizon of stable production, which was seen as benefit to both Canfor and its customers. These efforts resulted in the signing of a five-year agreement with the PPWC and discussions continue with the CEP. In cooperation with the IWA, Canfor's Wood Products operations moved to incorporating third shifts at its sawmills. In 2002, third shifts were introduced at the company's Fort St. James and Rustad sawmills and a third shift was negotiated for the Fort. St. John facility. This move was seen as creating stable jobs at the sawmills while generating the most efficient output from the mill asset. Third shifts were already in place at Isle Pierre and Polar operations.

Safety continues to be a priority at Canfor from the senior executives within the company to the hourly workers on the mill floor. While the Company's results when compared to the B.C. forest industry are good, nevertheless solid improvement occurred this year. In addition, Canfor commenced benchmarking our results against other industries which has demonstrated that we still have opportunities for further improvement.

The Canfor President's Safety Award process was revised in 2002 to include the review of the company's woodlands operations. As a result, an Interior Woodlands Health and Safety Award was designed to promote safe work practices among Canfor's salaried woodlands employees and promote contractor safety to the contractors working in Canfor woodlands operations.

This year's winners of the President's Safety Award were Intercontinental Pulp Mill in the over 400,000 hour category, and the Taylor sawmill in the under 400,000 hour category. The Peace Woodlands group were the winners of the new Interior Woodlands Health and Safety award.

At Canfor, we view our long-standing commitment to the communities in which we operate as a two way street. "Our roots are in this community" is as much about actively including the people who live and work in these regions as part of our day-to-day business as it is about the company's participation and support for community programs and organizations.

> **Canfor makes it a priority to tell our story to the people in our communities**

Canfor makes it a priority to tell our story to the people in our communities and people visiting our operating areas and bring them up to speed with the opportunities and challenges we currently face in the forest industry. In 2002, we expanded the Canfor Tour Program to make it one of the most popular places to experience the forest industry in the province of British Columbia. From May until September, Canfor shared information about our current practices and future direction with the over 1500 people who toured through our Prince George and Houston operations. In addition, the tour program included visits from over 30 school groups comprised of students from preschool to university who, we hope left with a better understanding of the industry and the role that it plays in the local economy.

Canfor also released the 5th edition of the popularly sought Canfor Recreation Map in two versions in 2002. The maps cover the roads and sites of interest in the Houston, Fort St. James, Vanderhoof and Prince George forestlands entrusted in our care. With the goal of helping make the forests more accessible to residents and visitors of these areas, we provided a set of current and detailed recreation maps to the public free of charge.

In addition to opening our doors to the public to help in the understanding of our business, Canfor continues to play a very active role with community and charity organizations throughout British Columbia and Alberta. Despite 2002 being a difficult year for the forestry sector, Canfor's United Way Campaign in 2002 resulted in record donations on behalf of the company and its employees and the Salvation Army granted Canfor membership in the "Founder's Circle" for the company's contributions, which made equipment like the Emergency Response Vehicle available to communities in northern British Columbia. Education also remains a priority for Canfor. In addition to providing the funding for capital projects such as the student housing complex at the Grande Prairie Regional College, the company continues to contribute to scholarships and bursaries at the high school, undergraduate and post graduate levels to assist students in furthering their education.

Summary of Operating Results

Year ended December 31	2002	2001
Sales volume – major products		
Lumber – millions of board feet (MMfbm) [(2)]	2,817.3	2,265.9
Plywood – million square feet, 3/8" basis (000 Msf 3/8") [(2)]	162.0	161.6
Pulp – thousands of metric tonnes (000 mt) [(3)]	993.5	940.1
Specialty Kraft Paper – thousands of metric tonnes (000 mt)	108.9	106.7
Logs – thousands of cubic metres (000 m³)	1,228.9	1,240.8
(millions of dollars)		
Net sales		
Wood Products	$ 1,348.1	$ 1,192.1
Pulp Products	466.6	499.5
Pulp and Specialty Kraft Paper	175.0	177.2
Coastal Operations	122.6	116.9
Total net sales	$ 2,112.3	$ 1,985.7
Segmented operating income (loss)		
Wood Products	$ 70.8	$ 74.9
Pulp Products	19.2	31.4
Pulp and Specialty Kraft Paper	(6.5)	(7.3)
Coastal Operations	5.7	(6.8)
Total segmented operating income	89.2	92.2
Non-segmented income (expenses)		
Non-segmented expenses	(34.1)	(29.7)
Equity in income of affiliated companies	5.0	1.1
Net interest expense	(59.2)	(64.2)
Other income (expense)	9.0	(0.3)
Unusual items	–	8.5
Total non-segmented expenses	(79.3)	(84.6)
Net income before income taxes	9.9	7.6
Income tax recovery	1.6	18.8
Net income	$ 11.5	$ 26.4
Cash flow from operating activities	$ 144.4	$ 118.8
(dollars per common share)		
Earnings per share, basic and diluted	$ 0.07	$ 0.27

Quarterly Financial Information

	2002				2001			
	1st	2nd	3rd	4th	1st	2nd	3rd	4th
Sales and income (millions of dollars)								
Net sales	$ 505.9	$ 577.0	$ 548.9	$ 480.5	$ 481.6	$ 511.2	$ 535.3	$ 457.6
Net income (loss)	11.1	70.2	(11.8)	(58.0)	18.8	10.1	19.6	(22.1)
Net income (loss) per common share (dollars)								
Basic	0.12	0.85	(0.16)	(0.73)	0.22	0.11	0.23	(0.29)
Diluted	0.12	0.75	(0.16)	(0.73)	0.21	0.11	0.21	(0.29)

(1) Certain comparative figures have been reclassified to conform to the 2002 presentation.
(2) Lumber and plywood sales volume represents Canfor production only.
(3) Pulp sales volume excludes Howe Sound Pulp and Paper Limited Partnership's sales volume of 343.5 (000 mt) in 2002 and 338.5 (000 mt) in 2001.

The Management's Discussion and Analysis (MD&A) provides a review of the significant developments that have impacted Canfor's performance during 2002 relative to 2001. Factors that could impact future operations are also discussed. These factors may be influenced by known and unknown risks and uncertainties that could cause the actual results to be materially different from those stated in this discussion. In addition to the risks and uncertainties discussed at the end of this MD&A, factors that could have a material impact on any future oriented statements made herein include, but are not limited to: general economic, market and business conditions; product selling prices; raw material and operating costs; foreign exchange rates; changes in law and public policy; and opportunities available to or pursued by Canfor.

Throughout this discussion, reference is made to EBITDA (operating income before amortization), which Canfor considers to be a key performance indicator of each operating segment and the Company as a whole. All financial references are in millions of Canadian dollars unless otherwise noted.

Overview of 2002

2002 was a challenging year for Canfor and the entire forest products industry. Lowest prices in a decade for both lumber and pulp, combined with punishing countervailing and anti-dumping duties initiated by the protectionists in the US lumber industry, had a substantial impact on the Company's results. Faced with these challenges, management is taking the necessary steps to improve the Company's competitive position.

Highlights of 2002

- Achieved record lumber production of 3 billion board feet
- Obtained the largest Sustainable Forestry Initiative® (SFI) certification in Canada
- Rustad sawmill was the first Wood Products processing facility to receive ISO 14001 certification of its Environment Management System (EMS)
- Wood Products segment reduced conversion costs by 7%
- Received "Highest Rated Pulp Supplier" award from The Blandin Paper Company
- Achieved record pulp production of over one million tonnes

In the fourth quarter of 2002, Canfor announced a company-wide Cost Reduction/Margin Improvement (CRMI) Program, targeted to deliver $150 million in annualized benefits by the fourth quarter of 2003. The following table summarizes CRMI targets by business segment:

Business Segment	Structural Improvement Targets $ millions	Capital Required $ millions	Net FTE Reduction [2]
Wood Products	$ 95	$ 76	285
Pulp and Paper Group	42	16	54
Coastal Operations	3	–	41
Centralized Services[1]	5	6	27
Corporate	5	–	7
TOTAL	$150	$ 98	414

(1) Consists of Technology and Research Group, Sourcing and Centralized Accounting Services. For reporting purposes these savings are separated out and allocated back to the business segments.
(2) Total of 414 consists of 278 hourly and 136 salaried employees and represents 7% of the entire workforce. FTE = full time equivalent.

Canfor continues to focus on its core Wood Products business with the objective of being among the lowest cost producers in the industry. During 2002, significant steps were taken towards achieving that goal, including operational improvements at all sawmills, third shifts at both the Fort St. James and Rustad sawmills and capital investments to install wane optimizers and dry kilns. On January 23, 2003, the Company announced the closure of the Taylor and Upper Fraser sawmills and the addition of third shifts at the Fort St. John and Prince George sawmills. This move is in keeping with Canfor's strategy to operate all sawmills on 3 shifts or at maximum capacity. With the completion of these 2 projects, 6 of 11 sawmills will be operating with 3 shifts. In addition, further analysis on adding a third shift at the Clear Lake sawmill and increasing production at the Houston operation is currently underway. Decisions based on this analysis will be disclosed with the Company's first quarter 2003 results. A strategic review of BC Peace Region and Alberta sawmills will also be complete in the second quarter of 2003, again, with the objective of maximizing capital utilization and efficiency.

One of Canfor's key strengths is the high quality fibre that is the basis from which it has built a reputation as a supplier of superior pulp, paper and lumber products. With the provincial forest policy changes expected this spring, and a shift towards more flexible, more competitive timber and log markets, in 2002, Canfor created a separate Fibre Management Group to ensure fibre support for its processing facilities, while maximizing the financial contribution of woodlands to the Company.

Achieving lower production costs and consistent quality are also key to the success of the Pulp and Paper business. The Company has focused its attention on conversion costs, identified high-return energy projects for its mills to reduce energy consumption, and redesigned its maintenance program to realize significant cost savings while increasing production capacity. Paper consistency and quality were a major focus during the year, with a significant improvement achieved after adjustments made to the paper machine during the October maintenance shutdown. This positive trend has continued into 2003.

The softwood lumber dispute remained unresolved in 2002 and continues to significantly impact Canfor's results. During the year, the Company paid $105 million in cash duties and $9 million in related legal fees. On July 11, 2002, Canfor filed a Statement of Claim against the United States government under Chapter 11 of the North America Free Trade Agreement. The claim alleges that the conduct of the United States, with respect to the softwood lumber dispute, and particularly its treatment of Canfor in the preliminary and final countervailing and anti-dumping determinations issued by the United States Department of Commerce, were arbitrary, unreasonable and discriminatory. Canfor appointed Frank McKenna as its representative on the Tribunal adjudicating the Company's Statement of Claim. The US has appointed Conrad Harper, a lawyer with the firm of Simpson, Thacher & Bartlett, New York.

While management is cautiously optimistic about a negotiated solution to the softwood lumber dispute, the Company is prepared to continue to pursue all legal remedies if required.

Summary

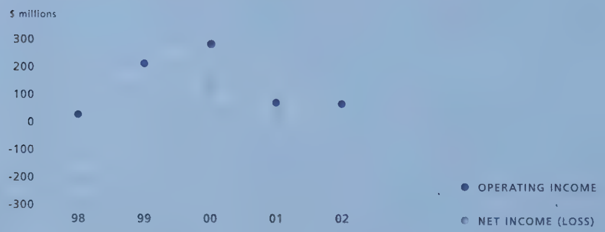
The Company is moving forward into 2003 with a solid foundation for improved results. Management has identified the actions required to drive costs down and improve margins in all areas of the business. An aggressive timeline for implementation is in place and management incentives are tied directly to achieving these objectives. In addition, commodity prices are beginning to rebound. The February and March announced pulp price increases have held, world pulp inventories are down and lumber prices have been much stronger in recent weeks, with random length pricing up by US $39 per thousand board feet between January 3rd and February 12th. Canfor is able to take full advantage of these price improvements as the Company is achieving record production levels in both lumber and pulp, with 3 billion board feet of lumber and one million tonnes of pulp produced in 2002.

Finally, there has never been stronger momentum toward fundamental policy reform than is now being seen in BC. These changes should help to resolve trade frictions with the US and encourage the BC industry to restructure and respond to the competitive realities of the global marketplace.

Operating Results

The following discussion of Canfor's operating results relates to the operating segments and the non-segmented items as per the Statement of Segmented Information in its Financial Statements. Canfor's operations include the following operating segments: Wood Products, Pulp Products, Pulp and Specialty Kraft Paper and Coastal Operations.

Net income and operating income



WOOD PRODUCTS

Goal

> *Achieve top quartile cost structure measured against North American producers;*
>
> *Optimize value from sawmill assets and fibre resources;*
>
> *Meet customer needs for high-quality, eco-certified, branded products.*

The segment consists of logging and forestry operations, which harvest over 7.9 million cubic metres of allowable annual cut. In 2002, the forest operations supported 13 sawmills, a plywood manufacturing facility, 3 re-manufacturing plants, 2 whole-log chipping plants, and a wood treatment plant. The operations have the annual capacity to produce over 3 billion board feet of lumber, 174 million square feet of plywood (3/8" basis) and over 1.8 million oven-dried tonnes of wood chips. The operations, employing approximately 3,500 people, are located within the Prince George and Peace regions of British Columbia and in northern Alberta. Canfor's wood products marketing group is headquartered in Vancouver. The segment also includes the Panel and Fibre operation, located in New Westminster, British Columbia, which was previously included in the Coastal Operations segment.

Summarized results for the Wood Products segment for 2002 and 2001 are as follows:

(millions of dollars)	2002	2001*
Net sales	**$ 1,348.1**	$ 1,192.1
Operating income	**$ 70.8**	$ 74.9
EBITDA	**$ 120.7**	$ 117.1
EBITDA margin	**9%**	10%
Capital expenditures	**$ 35.4**	$ 17.8
Lumber shipments (millions of board feet)		
Canfor produced	**2,817**	2,266
Other producers	**278**	274
Plywood shipments (millions of square feet – 3/8" basis)	**162**	162
Chip shipments (thousands of oven-dried tonnes)	**1,666**	1,372
Hardboard shipments (millions of square feet – 3/8" basis)	**37**	35
Refined fibre and fibremat shipments (thousands of oven-dried metric tonnes)	**39**	40
Average random length 2"x 4" SPF lumber price (US$ per thousand board feet)	**$ 237**	$ 251
Average US dollar to one Canadian dollar	**$ 0.637**	$ 0.646

* Restated to include the Panel and Fibre operation

The segment's operating income and EBITDA for 2002 are after providing for mill closure costs and termination benefits of $22.6 million. As the above table shows, net sales increased by 13% over the prior year, in spite of the 6% decrease in average 2"x 4" prices. This is a reflection of the increased production in the year, which resulted in a 24% increase in lumber shipments compared to 2001.

Following the company-wide Cost Reduction/Margin Improvement Program announced in October 2002, an extensive review of mill configurations, relative capacity, log costs, fibre supply issues, capital needs, product mix, market requirements and overall cost structure was performed. The difficult decision was made to close 2 sawmills. The Upper Fraser sawmill, which is negatively impacted by high fibre and transportation costs, and the Taylor sawmill, which has less potential to be fully cost competitive due to its age and smaller size, will close during the third quarter of 2003. At the same time, $40 million of capital projects were approved to upgrade the Fort St. John and Prince George sawmills, which will allow them to run 3

shifts. As a result of the additional shifts and other initiatives, Canfor's overall production capacity will not be reduced going forward, and employment opportunities will be created for approximately 110 of the employees from Upper Fraser and Taylor.

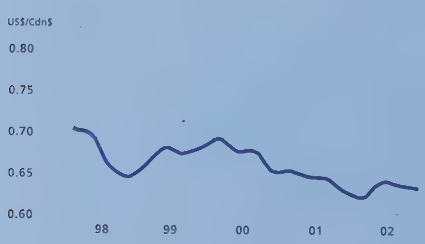
Markets

Lumber market conditions were positive for the first half of 2002, but deteriorated steadily during the second half of the year. Prices for North American 2"x 4" Random Length (RL) averaged US $264 per thousand board feet (Mfbm) in the first half of the year, which was considerably higher than the average price in the fourth quarter of 2001. Although demand for lumber remained relatively strong throughout 2002, an abundance of supply kept average prices low. Prices declined sharply, to an average of US $209/Mfbm, during the second half of the year. The average 2"x 4" price for all of 2002 was US $237/Mfbm, which is 6% below the previous year's average of US $251/Mfbm.

On May 22, 2002, the US imposed countervailing (CVD) and anti-dumping (ADD) duties of 18.79% and 8.43%, respectively, on Canadian lumber shipments to the US. Canfor was assessed a specific ADD rate of 5.96% based on its product shipment profile during the period of review, which resulted in a total duty of 24.75%. The imposition of these duties significantly reduced the competitiveness of Canadian lumber producers relative to other US suppliers. In order to remain competitive and maintain market share, Canadian SPF (spruce-pine-fir) lumber producers reduced operating costs by operating their sawmills at much higher levels and for longer time periods than in 2001. As a result, total Canadian SPF production increased by 10%, or 2 billion board feet, over 2001, when production levels were significantly lower than normal because most mills took extensive curtailment in response to the market conditions at the time.

The impact of low mortgage rates and relatively strong consumer confidence in 2002 caused US housing starts to be at their highest level since 1986, which resulted in high demand for lumber during the year. Single-family housing starts, at 1.36 million, were 6.8% higher than in 2001 and total housing starts, at 1.7 million, were up by 6.4%. The US South, a major user of SPF lumber and the region that builds the highest number of houses, recorded the greatest increase in housing starts over 2001. Other areas of consumption were also strong, such as lumber used in home repairs and remodeling, which rose by approximately 4% over 2001.

US$/Cdn$ average annual exchange rate



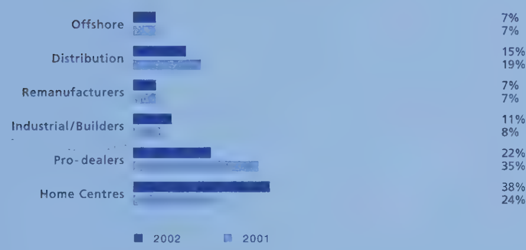
North American lumber prices* and housing starts

** Average 2"x 4" SPF random length price (F.O.B. Mill) - Source Random Lengths publication.*

The Japanese economy was stagnant in 2002, which was reflected in a 2% decline in total housing starts from the previous year. However, construction of houses requiring 2"x 4" lumber actually increased by over 2% from the 2001 level. As a result of continued efforts to diversify from the US market, Canfor's shipments to Japan increased by 15% in 2002 over 2001 levels. Demand was strong in other Asian markets, and Canfor nearly doubled its shipments to Korea, Taiwan and China over 2001 levels. The Chinese market continues to expand as interest in North American style housing grows. Much effort is currently being made to assist China in developing building codes, which will allow for more wood to be used in home construction as opposed to concrete or masonry. Canfor continues to supply a significant portion of the Chinese market and has developed marketing strategies to gain share as interest in wood housing grows.

Lumber sales by region

Lumber sales by market segment



Lumber shipments from Canfor's operations increased by 24%, or 551 million board feet, in 2002, which is partly a reflection of the high level of production curtailment taken in 2001. Of this increase, over 500 million board feet was shipped to the US market. During 2002, Canfor continued to focus its attention on the growing home centre market, which creates a strong demand for higher-value, appearance-grade lumber, and on the home construction market, including the expanding housing component segment of that market.

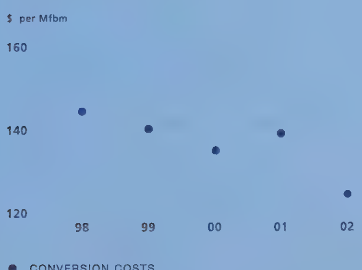
Operating Performance

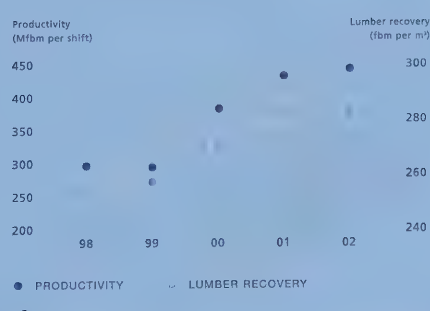
With the expiration of the quota restrictions in 2001 and the implementation of the CVD and ADD in 2002, the Wood Products segment positioned itself to reduce costs and gain market share by running at near full capacity in 2002. This strategy is in sharp contrast to the operating conditions in 2001, when the sawmills curtailed production by 658 million board feet. In response to the extreme price pressure experienced in the latter half of 2002, the segment focused on managing the product mix in order to minimize its exposure to the ADD.

On May 16, 2002, the US International Trade Commission, in its final determination on the existence of injury or threat of injury, ruled that Canadian producers only posed a "threat of injury" to American lumber companies. The ruling resulted in all previously accrued duties being reversed, which, for Canfor, meant a retroactive adjustment of $45.8 million for duties accrued in 2001 and a $14.7 million reversal of duties accrued in the first quarter of 2002. The ruling resulted in the imposition of CVD and ADD, requiring cash deposits, effective from May 22, 2002. In the final determination of the ADD rates, Canfor received the second lowest rate in Canada of 5.96% versus the industry average of 8.43%, which positioned Canfor positively among Canadian producers. While the cash payments for the ADD are being made at the assessed rate of 5.96%, the ADD expense has been accrued at an average rate of 5.6% for 2002, which is a best estimate of the rate applicable to Canfor's product shipment profile, as determined by applying the Department of Commerce's (DOC) methodology. Canfor expects that the DOC will officially reassess the rate during its administrative review process. The difference between the assessed rate and the accrued rate amounted to $1.1 million in 2002, which is being recorded as a long-term receivable. Total cash payments of $105 million were made for the combined duties in 2002.

A significant reduction in conversion costs was fueled by production facilities running at near full capacity in 2002. To further position the Wood Products segment as a long-term, low-cost producer, several initiatives were implemented in 2002 to upgrade mill optimization technology, which will improve productivity, lumber recovery and production of high-value lumber going forward.

Operating Improvements





There were many operational improvements during 2002, which should not be overshadowed by the impact of the low lumber prices. Significant improvements over 2001 were made in the following areas:

- 3% increase in productivity
- addition of third shifts at 2 sawmills
- 7% decrease in conversion costs (per Mfbm)
- 22% increase in value-added products, such as those sold to the home centres and the Japanese market, as well as specialty products like finger-jointed, fascia and machine stress-rated lumber.

The segment also includes the Panel and Fibre operation, which is focused on being the supplier of choice for high quality, value-added products in the decorative wall paneling, baled fibre, hydroseeding and woodmat industries. Raw materials for the wall paneling and fibre lines are from recycled urban wood waste. Panel and Fibre performed well in 2002, but operating income declined by 19% from 2001, primarily as a result of high energy costs. Sales of the ECOFIBRE™ product were especially high compared to the previous year due to the installation of a new bagger in the summer, which doubled production capacity. A large volume of the product was also sold to Colorado following the forest fires in the summer of 2002. At the end of the year, Panel and Fibre began a capital project to convert their hardboard press, which will result in a 25% increase in panel production capacity in 2003.

Risks

MOUNTAIN PINE BEETLE The mountain pine beetle currently poses a significant threat to the lodgepole pine forests in the west-central interior region of British Columbia, which is within Canfor's operating area. Risk and uncertainty around the mountain pine beetle exist due to geographic and temporal factors, fibre quality concerns, and manufacturing constraints. Based on the current location of the infestation, the availability of suitable host material and the prevailing wind direction indicate that the potential exists for an increase in the portion of beetle-attacked timber in Canfor's existing operating area.

When timber is infested by mountain pine beetle, it goes through several distinctive phases of quality change. Immediately after infestation, a blue stain starts to grow in the cambium area *(a cell layer in the outer part of the tree that produces new wood for the growth of the tree)* and spreads in the sapwood *(the outer layers of growth, between the bark and the dormant heartwood)*. Much of the sapwood is chipped during the manufacturing process and is not deemed to be a quality issue for pulp and paper production, but the blue stain will limit premium lumber grades into Japan (J-Grade). After one year, the tree dies and the beetles move on. The tree then starts to dry and, as a result, checks in the wood *(lengthwise separation of wood, normally occurring across or through the rings of annual growth)* develop, and get larger over time. Research needs to be conducted on the rate of deterioration due to checking in the west-central British Columbia geographic area. A significant cold snap in the fall or early winter would stop the spread of the infestation, but failing that, a continuing beetle epidemic would eventually burn itself out as it works its way through all of the mature pine in the area. If this occurs, the reduced availability of mature pine could significantly impact the fibre supply picture, lowering allowable annual cuts by up to 10%.

Lodgepole pine accounts for 25% of the total timber volume harvested in British Columbia and 50% of the total timber volume harvested by Canfor in the region. The present outbreak covers over 9 million hectares of land or 10% of the province's land base. This is an increase of 28% from the area infected in 2001 within Canfor's operating area. Canfor is working with the Ministry of Forests and other operators in the area to implement an aggressive program to mitigate the spread of infestation by redirecting planned timber development to infected regions over the next five years. As a result, approximately 80% of Canfor's planned log consumption in the Prince George region in 2003 will be from beetle-infested stands.

The average diameter of lodgepole pine logs tends to be smaller than traditional harvests and does not match well with existing sawmill equipment in the Prince George region. This issue is being addressed through realignment of manufacturing facilities to fit the future supply. In the short-term, Canfor has announced major capital expenditures to realign the Prince George region manufacturing capabilities to accommodate the increase in fibre from beetle-infested logs. However, if the outbreak continues to spread, the potential implications to Canfor include a change in lumber product mix, increased costs and a potential decrease in the quality of lumber and chips produced.

SOFTWOOD LUMBER AGREEMENT The US Department of Commerce has issued a draft of Forest Policy Reforms to eliminate countervail duties. The Canadian stance is fragmented. A majority of the provinces are of the opinion that industry should aim for a settlement and negotiate on reforms, while a minority believes that Canada is winning with the World Trade Organization and should continue along the legal route. Ongoing discussions towards a settlement framework remain a possibility. However, the prudent approach going forward is to work with the known countervailing duty and anti-dumping structure in place.

Outlook

Strong US housing starts remain one of the few bright spots in the economy. The main drivers continue to be attractive interest rates and growth in personal income levels, in spite of a sluggish job market. Demand for lumber in the US is expected to remain relatively strong into 2003, but prices are not expected to improve until the third quarter. Canfor will remain focused on growing the home centre market and the rapidly growing housing component market, while also continuing to supply the traditional housing construction market.

Low lumber prices and competitive cost pressures in the context of the continuing trade dispute with the US have necessitated a thorough review of Canfor's manufacturing assets, relative cost position and capital efficiency. As discussed above, closure of high-cost manufacturing facilities, capital investments to realign existing facilities with changing fibre and technologies, and higher utilization of existing assets are planned for the upcoming year. All of these measures are part of the intensive Cost Reduction/Margin Improvement Program targeted to increase profitability of the Wood Products segment by $95 million annually, on an ongoing sustainable basis, as detailed below.

Initiative (millions of dollars)	**Capital Expenditure Required**	**Structural Improvement Targets**
Closure of Upper Fraser and Taylor mills, announced in January 2003	$40	$30
• 3rd shift added, and sawmill log line upgrades to Fort St. John and Prince George sawmills		
Installation of linear wane optimizers to improve grade out-turn and margins at 7 mills	$11	$18
• Already installed at Houston and Isle Pierre		
• Currently starting up at Polar, Fort St. James and Grande Prairie		
• Installation planned for Fort St. John and Chetwynd		
Reduction in FTEs		
• Associated with capital projects	$10	$11
• Non-capital FTE reduction of 50 people	N/A	$ 5
Kiln projects at Isle Pierre, Prince George and Polar sawmills	$ 7	$ 3
Fibre savings initiatives, achieved through	N/A	$20
• Log quality management		
• Hauling practices		
• Overhead spending reductions		
Other capital projects	$ 8	$ 8

With the realignment of manufacturing facilities, including the addition of third shifts at another 4 of Canfor's sawmills, the segment expects to increase its lumber capacity to 3.4 billion board feet by 2004. The increased capacity, combined with the Company's focused marketing expertise, established distribution systems and extensive fibre base, should allow Canfor to continue its strategy to grow with its valued customers for the long term.

PULP PRODUCTS

Goal

> *To be a low cost producer of the most consistent, superior strength reinforcing pulp.*

Canfor's pulp, which is produced from long northern British Columbia wood fibres, offers the strength sought by paper makers. This segment consists of the Intercontinental and Northwood pulp mills and a chemical operation, all located within five kilometres of each other in Prince George, British Columbia. The pulp mills have the annual capacity to produce approximately 860 thousand tonnes of premium pulp. The segment directly employs approximately 930 people. Also included in the Pulp Products segment is Canfor's pulp and paper marketing group, which is headquartered in Vancouver.

Summarized results of the Pulp Products segment for 2002 and 2001 are as follows:

(millions of dollars)	2002	2001
Net sales	**$ 466.6**	$ 499.5
Operating income	**$ 19.2**	$ 31.4
EBITDA	**$ 54.8**	$ 66.7
EBITDA margin	**12%**	13%
Capital expenditures	**$ 9.1**	$ 11.8
Average pulp price – delivered to Northern Europe (US$ per tonne)	**$ 462**	$ 537
Pulp shipments (thousands of tonnes)	**836**	792

The main reason for the decline in operating income was the 14% decrease in average pulp prices from the prior year. Additionally, operating income was reduced by $5.4 million of termination benefits, which were accrued as part of the company-wide Cost Reduction/Margin Improvement Program.

Markets

Pulp prices are quite susceptible to supply and demand imbalances, which cause price fluctuations. Economic uncertainty prevailed in 2002, particularly in the United States. List prices for pulp delivered to the Northern European market began the year at the US $460 per tonne level, but towards the end of the second quarter, demand for hardwood pulp from Asia and Europe strengthened to the point that inventories began to decline. Market pessimism in the latter part of 2001 gave way to renewed optimism and an increase in paper consumption triggered an increase in pulp demand. Consequently, the Northern European price for NBSK (Northern Bleached Softwood Kraft) pulp recovered from a low of US $435 per tonne in April to a high of US $490 per tonne in June.

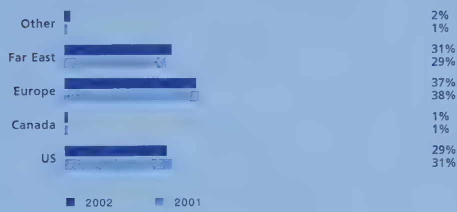
This recovery was short lived as falling stock markets reflected a return of consumer concerns and demand for pulp and paper products began to fall. Inventories started climbing halfway through the year, which caused a steady decline in prices beginning in September and culminated in a low of US $440 per tonne in December. NORSCAN (North American and Scandinavian) inventories were 1.6 million tonnes at the end of 2002. Although this level of inventory is still relatively high (1.5 million tonnes of NORSCAN pulp inventories is considered the market supply and demand equilibrium level), it was lower than the historical average for the period. Declining inventories, in combination with a shortage of pulp chips, which arose due to weather conditions in the Southeastern US and sawmill downtime in Eastern Canada, is having a positive impact on prices. In January 2003, Canfor announced a price increase, to US $480 per tonne, effective February 1st. In February, a further price increase, to US $520 per tonne, was announced, effective March 1, 2003.

NBSK pulp prices/chemical pulp producers inventories*

* *Average price paid by contract buyer, delivered to Northern Europe/NORSCAN Chemical Paper Grade Market Pulp Producer Inventories – Source: Forest Products Association Canada (FPAC).*

Pulp sales by region

(Includes pulp sales for both the Pulp and the Pulp and Specialty Kraft Paper segments)



With the low demand for pulp in North America and Europe throughout most of 2002, and the desire to maintain appropriately low inventory levels, Canfor continued to increase its presence in the Far East market. Although sales into the Far Eastern countries, especially to China, tend to occur at higher discounts from the Northern European benchmark price than other regions, this lower price is partially offset by significant savings on distribution costs to these countries, which results from the ships often being able to bring back other cargo on their return trip.

Operating Performance

Demand for pulp from Canfor's regular customers was relatively steady throughout the year. As a result, the mills were able to run at near full capacity, unlike in 2001 when significant production curtailments were taken in order to balance inventory levels. Overall productivity was excellent, with both the Northwood and Intercontinental mills achieving record production for the year. These productivity improvements can be attributed to improved equipment reliability and synergies resulting from best practices coming to fruition with the amalgamation of the legacy Northwood and Canfor mills.

The higher production rates had a significant impact on unit costs, which decreased by 9% from 2001. During 2001, unit costs were significantly higher than normal, as a result of the curtailments taken and the additional expense involved in restarting a mill after a shutdown. A 21% decrease in fibre costs, primarily arising from the lower pulp prices, together with the impact of various spending reduction initiatives, also contributed to the reduced costs in 2002.

Risk

The main business risks for the Pulp segment center around pulp pricing, fibre supply and energy prices. Availability and cost of the fibre used to make pulp is another risk area, particularly during times of sawmill curtailment. However, Canfor is in a good position to control its fibre supply in the central interior of British Columbia. Energy prices are also impacted by supply and demand, as was seen by the dramatic increase in natural gas prices after the market deregulation in the United States. Electricity could potentially follow in the same path, which could have a major impact on production costs. However, the segment is mitigating the risk of potential increases in energy costs by increasing its percentage of self-generated electricity. Additional energy reduction projects to reduce natural gas requirements are planned for 2003.

Outlook

Weak global economic conditions are expected to result in a continuation of low prices in 2003 overall, but a gradual improvement is anticipated to evolve over the course of the year. China returned to the market to a large degree in the latter part of 2002, which helped to support price increases in early 2003. Lower inventory levels, resulting from the continuing chip shortage and sawmill shutdowns, are expected to contribute to a moderate rise in prices. The expectation is for pulp prices to gradually increase throughout the year, as pulp supply and demand equilibrium is restored. The segment's strategy is to run at full capacity whenever market conditions permit, in order to minimize overall cost per tonne. There is some indication from market forecasting groups that the pulp market may pick up in 2004/2005.

As part of Canfor's overall strategy of cost reduction, and to take advantage of synergies on the pulp line in the Prince George Pulp and Paper Mill, effective January 1, 2003, the management of the Pulp Products and the Pulp and Specialty Kraft Paper segments have been realigned to form one decision-making unit, which will be reported on as one segment ("Pulp and Paper") beginning in the first quarter of 2003. The newly combined Pulp and Paper segment has undergone a review of its operations and has identified a number of initiatives that are expected to produce ongoing annualized benefits of approximately $42 million by the end of 2003, as detailed below.

Initiative (millions of dollars)	**Capital Expenditure Required**	**Structural Improvement Targets**
12 separate energy reduction projects, which once completed will reduce overall natural gas consumption by 20%	$ 8	$ 8
Paper machine margin and productivity improvements	N/A	$ 11
Maintenance shutdown/reliability savings through reduced annual maintenance downtime	N/A	
• This will increase production by 24,000 tonnes		$ 10
• Best practices during a shutdown		$ 4
Non-capital FTE reduction of 50 people	N/A	$ 5
Other capital projects	$ 8	$ 3
General spending reductions	N/A	$ 1

PULP AND SPECIALTY KRAFT PAPER

Goal

> *To be a world-class manufacturer of high-value, high performance kraft papers;*

> *Optimize profit through growth in niche markets.*

This segment, which consists of the Prince George Pulp and Paper Mill, will have the capacity, at optimum product mix levels, to produce 135 thousand tonnes of kraft paper and 142 thousand tonnes of pulp in 2003. The mill is located in Prince George, British Columbia and directly employs approximately 400 people.

Summarized results of the Pulp and Specialty Kraft Paper segment for 2002 and 2001 are as follows:

(millions of dollars)	2002	2001
Net sales	$ 175.0	$ 177.2
Operating loss	$ (6.5)	$ (7.3)
EBITDA	$ 8.2	$ 6.9
EBITDA margin	5%	4%
Capital expenditures	$ 13.7	$ 14.7
Average Canfor paper selling prices (Cdn$ per tonne)	$ 842	$ 840
Average pulp price – delivered to Northern Europe (US$ per tonne)	$ 462	$ 537
Specialty kraft paper shipments (thousands of tonnes)	109	107
Pulp shipments (thousands of tonnes)	158	148

The segment's loss for the year includes a $1.5 million provision for termination benefits, which was recorded as part of the company-wide Cost Reduction/Margin Improvement Program. There were significant improvements in the paper line during the latter part of the year, which is reflected in the increase in EBITDA from 2001, despite the impact of the lower pulp prices.

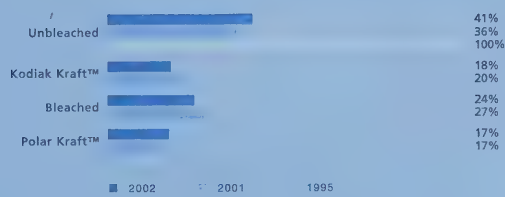
Markets

Demand for the segment's paper products was steady in 2002. Paper pricing is generally constant and is subject to only relatively minor cyclical swings in comparison to pulp prices. Price increases were achieved in the second half of the year for both unbleached and bleached paper products in North America and in the bleached grades sold to the offshore market.

Canfor has been able to carve out markets with independent converters and flexible packaging users for POLAR KRAFT™ and KODIAK KRAFT™ high performance papers. As anticipated, there has been a significant growth in demand for high performance papers in North America, as consumers increasingly move away from traditional multi-wall papers. High performance paper offers stronger bags while using less paper, which reduces costs for these manufacturers. The segment's strategic direction to produce high performance and specialty papers continues to be well received by customers. High performance paper is now the largest growth area in all major paper markets and this trend is expected to continue in the coming year. Specialty grades of pulp are targeted for niche markets that value the superior quality of long-fibre pulp that Canfor produces.

Paper sales by region

Paper sales by product



Operating Performance

The paper machine underwent a major upgrade in 2001, and mill personnel have been going through a significant learning curve during the start-up phase. Manufacturing performance was poor in the first half of 2002. Paper machine operations struggled with several very difficult technical issues, which had a significant effect on quality, coupled with poor mechanical reliability and the steep learning curve required to resolve these issues. Trouble-shooting the quality issues took considerable time and effort, and required the machine to run at reduced speeds until key modifications could be made at the end of the third quarter. Since the modifications, productivity has started to trend upwards and improvements in quality have been achieved. Performance showed steady improvement in the last half of the year, and significant progress has been made in terms of machine reliability. Additional skilled resources have been acquired and there has been a notable increase in the level of operational understanding and papermaking skills. Work continues on optimizing productivity on the machine and in all sectors of the paper business.

The total output of the mill averaged below target levels set for 2002. The interruptions on the paper machine and a growing shift from bleached to unbleached pulp production compromised mill productivity. However, as the paper machine's operations improved, a better balance with the pulp operations was achieved and total output of the mill has been trending upwards. The mill produced at target levels in the fourth quarter, and further optimization to balance between product mix (paper versus pulp) and grade mix (bleached versus unbleached) is continuing.

The mill's profitability is significantly affected by high energy costs. Several projects have been successfully implemented or developed during 2002 that have reduced energy usage. Other projects are currently being evaluated which could result in a significant decrease in energy costs and greatly improve the business's competitive position.

Risk

Market risk for paper is relatively low. While overall paper consumption is declining, the market segments that Canfor has targeted, particularly the high performance paper market in North America, are experiencing growth. The biggest risk factor that could affect the segment's stated objectives and profitability levels is the timing of achieving production and quality targets on the paper machine.

Outlook

The business unit is well positioned to become a significant supplier to the high performance paper market, and is the sole North American supplier of high performance bleached kraft paper. With the improvements that were seen in the last half of the year, the development of higher value products, such as low porosity paper, is now being pursued. Work is in progress to maximize profitability by rationalizing the customer base and focusing the grade mix toward higher value products, which the paper machine is capable of producing. The strategic direction continues to be the growth of bleached and unbleached high performance paper products, which consistently provide the highest return for the business. As the operational and quality issues on the paper machine continue to improve and prime paper production increases, the paper line is expected to generate consistent profits.

COASTAL OPERATIONS

Goal

> *Maintain a profitable, market-sensitive, cost-competitive logging and fibre management operation.*

Canfor's Coastal Operations segment is comprised of the Coastal Logging operations, which includes the Englewood and Mainland logging operations and the Coast Fibre Supply operation. The Coastal Logging operation has an allowable annual cut of 1.5 million cubic metres, of which 1.4 million was harvested in 2002. The segment directly employs approximately 430 people.

Summarized results of the Coastal Operations segment for 2002 and 2001 are as follows:

(millions of dollars)	2002	2001*
Net sales	$ 122.6	$ 116.9
Operating income (loss)	$ 5.7	$ (6.8)
EBITDA	$ 13.6	$ 2.4
EBITDA margin	11%	2%
Capital expenditures	$ 6.4	$ 7.2
Log shipments (thousands of cubic metres)	1,229	1,241

* Restated to exclude the Panel and Fibre operation, as discussed in the Wood Products section.

The operating income for 2002 is after a $2.7 million provision for termination benefits, which was accrued as part of the company-wide Cost Reduction/Margin Improvement Program. The increase in the segment's EBITDA over the prior year is reflective of the improvement in market conditions, as discussed below.

Markets

After virtually collapsing in the last quarter of 2001, the coastal log market showed some signs of improvement in 2002. The market was still affected by the continuing uncertainty surrounding the softwood lumber dispute, as well as by the declining pulp markets and poor economic conditions in Japan. However, Canfor was able to take advantage of the limited log supply available on the Coast, which resulted from the widespread shutdowns and reduced activity of other coastal logging operators. Demand for Canfor's products remained steady throughout the year and the average log price strengthened by approximately $10 per cubic metre over the previous year.

Operating Performance

As a result of the improved market conditions, the Coastal Logging operation was able to operate at full capacity whenever weather conditions permitted, in contrast to the previous year when weak demand forced it to curtail production by 18% of its allowable annual cut. Operating income for the segment increased by $12.5 million from 2001 to 2002. The higher production levels had a positive impact on production costs, which are very dependent on logging volume. However, although camp costs were 4% lower than the previous year, stumpage fees increased by 16% as a result of the product mix and the impact of higher log prices.

Other operational achievements in 2002 included significant improvements in safety, increased construction of roads and bridges, and meeting targets for standing timber inventory and environmental management.

Risk

The reduction in the number of manufacturing mills on the Coast, together with the uncertainty in the Asian market, will have a major impact on log markets. Going forward, Canfor will continue to monitor its competitors' operating levels and adjust its strategy accordingly. In addition to pricing and market demand, the critical factor that will impact profitability going forward is Canfor's ability to continue to drive down costs.

Outlook

The coastal fibre business climate is one of consolidation and shrinking customer base, which has created a highly competitive supply-side culture with an emphasis on quality, availability and reliability of supply. Under these conditions, the segment expects to accomplish its long-term strategy for growth through strategic changes in its operations and an increased focus on individual customer needs and timely delivery of product.

As part of the company-wide Cost Reduction/Margin Improvement Program, the segment will focus on such areas as rationalization of company and contractor operations and various cost reduction initiatives, which together are anticipated to produce approximately $3 million in ongoing annualized benefits by the end of 2003.

Initiative (millions of dollars)	**Capital Expenditure Required**	**Structural Improvement Targets**
Non-capital FTE reductions • 29 positions in logging operations • 12 salaried positions	N/A	$ 3

Non-Segmented Expenses

Non-segmented expenses, which are comprised of corporate costs, information technology costs and research and development costs, increased by $4.4 million from 2001 to 2002. The majority of the increase relates to legal fees associated with the NAFTA lawsuit (discussed below), the write-off of development costs for a cancelled information technology project and the settlement of a contractual dispute that predated the acquisition of Northwood in 1999.

A $1 million provision for termination benefits also contributed to the increase in expenses in 2002. As part of the company-wide Cost Reduction/Margin Improvement Program, Canfor's corporate department has identified specific initiatives that are expected to reduce costs by approximately $5 million per year on an ongoing basis. An additional $5 million of annualized savings are expected to be achieved by Canfor's centralized service departments, which will be allocated back to the operating segments. The details of the initiatives are outlined below.

Initiative (millions of dollars)	**Capital Expenditure Required**	**Structural Improvement Targets**
Corporate Office	N/A	
• Non-capital FTE reduction of 7 people		$ 0.7
• Reduced consulting and professional fees		$ 3.0
• General spending reduction		$ 1.3
Technology and Research Group, Sourcing and Centralized Accounting Services	N/A	
• Non-capital FTE reduction of 27 people		$ 2.7
• Conversion from a mainframe to a client server environment		$ 2.0
• General spending reduction		$ 0.3

Research and Development

Canfor is committed to being a leader and innovator in the forest products industry, with continuous investment in research and development. The objective of Canfor's research and development group, the only corporately owned and operated forest products research facility of its type in British Columbia, is to enhance Canfor's competitive position through the development of innovative products and technologies. In 2002, the research and development group worked closely with marketing and operations on the following projects:

- high-value laminated wood products from low-value lumber;
- high-value wood product opportunities from underutilized species of fibre;
- increasing premium pulp quality and converting lower-value pulp into higher-value specialty grade pulp;
- development of high-margin paper products;
- increasing efficiencies in mill processes.

Canfor's research and development expenditures amounted to $2.4 million in 2002.

Affiliated Companies

Canfor's affiliated companies, which are accounted for on an equity basis, consist of Lakeland Mills Ltd., The Pas Lumber Company Ltd., Vernon Seed Orchard and Kyahwood Forest Products. Lakeland and The Pas operate sawmills in the Prince George region and supply wood chips to Canfor's pulp mills. Kyahwood, which is owned 49% by Canfor, is a value-added lumber facility in Moricetown, British Columbia. The combined income of these affiliates increased by $3.9 million from 2001 to 2002, mainly as a result of Lakeland and The Pas benefiting from the same reversal of the 2001 CVD/ADD accruals, as did Canfor's Wood Products segment.

Interest Expense

Net interest expense, as detailed in Note 13 to the Financial Statements, decreased by $5.0 million in 2002 from 2001, primarily as a result of reduced short-term borrowing, in combination with lower interest rates on Canfor's operating lines of credit.

Other Income

Other income of $9.0 million in 2002 was mainly comprised of an $11.4 million gain on the sale of property, which was the site of the Eburne sawmill that was closed down in 1998, partly offset by losses from a subsidiary in a non-core line of business. The unusual item in 2001 relates to an insurance claim settlement of $8.5 million from a fire at the Upper Fraser sawmill that occurred in 1997.

Income Taxes

Income taxes as detailed in Note 15 to the Financial Statements include the following:

On March 10, 2001, Canfor and Oji Paper Co., Ltd. (Oji) of Japan, its 50% co-venturer in the Howe Sound Pulp and Paper Limited (Howe Sound) joint venture, transferred the business of Howe Sound into a limited partnership, Howe Sound Pulp and Paper Limited Partnership (the Partnership). The Partnership continues to be jointly owned by Canfor and Oji and continues to carry on the existing operations of Howe Sound. As a result of the reorganization, Howe Sound was amalgamated with Canadian Forest Products Ltd. (CFP), Canfor's principal operating subsidiary, and approximately $643 million of tax losses of Howe Sound became available to reduce the future taxable income of CFP. CFP has 7 years in which to utilize these losses.

Also, as part of the reorganization, CFP made a payment of $60.2 million to the Partnership in 2001, which was applied to reduce its long-term debt. During 2002, CFP made additional payments, totaling $5.0 million, to the Partnership and has agreed to make further payments, up to a maximum of $57.1 million, as it utilizes the tax losses of Howe Sound. Canfor wrote off its interest in the joint venture in 1998 and no longer reflects its share of Howe Sound's results. Canfor's method of accounting for its interest in the Partnership has not changed as a result of the reorganization.

The income tax recovery of $1.6 million recorded in 2002 includes future income tax savings of $8.0 million (2001 – $6.3 million) arising from Canfor's share of the Partnership's current operating losses. The income tax recovery recorded in 2001 of $18.8 million was higher as a result of the recovery of $18.7 million of future income taxes, which arose from the Provincial Government of British Columbia's 3% reduction to the corporate tax rate. The phase-out of the provincial corporate capital tax, which began in 2001, was completed as of September 1, 2002, and resulted in a $1.8 million reduction in the 2002 expense as compared to the previous year.

In 2002, Canfor received a Notice of Assessment from the Income Taxation Branch of the British Columbia Ministry of Provincial Revenue with respect to property transfer taxes associated with the amalgamation described above. The notice denied CFP's claim for an exemption from property transfer tax resulting from the amalgamation of CFP and Howe Sound. The potential liability arising from this assessment, including accrued interest to December 31, 2002, is $10.4 million. In the opinion of management and counsel, the amalgamation qualifies for exemption from property transfer taxes and, therefore, CFP is vigorously contesting the assessment. A Notice of Objection has been filed and, as required by the Ministry, CFP has posted a Letter of Credit for the assessed amount plus accrued interest. No provision has been made for the amount, however the potential liability has been disclosed in the notes to the Financial Statements.

SUMMARY OF FINANCIAL POSITION

The following table summarizes Canfor's financial position as at the end of the years 2002 and 2001 and the cash flow related to the changes in financial position for those years.

(millions of dollars)	2002	2001
Net cash	$ 22.9	$ 30.2
Operating working capital	346.3	402.0
Current portion of long-term debt	(51.4)	(52.7)
Current portion of deferred reforestation	(38.8)	(33.9)
Income taxes payable	(5.8)	(1.2)
Net working capital	273.2	344.4
Long-term investments	94.7	71.3
Property, plant, equipment and timber	1,424.2	1,469.0
Deferred charges	139.3	159.9
Net assets	$ 1,931.4	$ 2,044.6
Long-term debt	$ 643.4	$ 714.7
Countervailing and anti-dumping duties provision	–	47.4
Deferred reforestation provision	42.3	42.3
Other long-term provisions and accruals	41.6	28.7
Future income taxes – net	154.5	147.0
Deferred credit	95.7	104.0
Common shareholders' equity	953.9	960.5
Total capitalization	$ 1,931.4	$ 2,044.6
Ratio of current assets to current liabilities	1.7:1	2.0:1
Ratio of net debt to common shareholders' equity	41:59	43:57
Cash generated from (used in)		
Operating activities	$ 144.4	$ 118.8
Dividends	(21.1)	(21.1)
Financing activities	(55.2)	77.8
Investing activities	(75.4)	(121.7)
Increase (decrease) in net cash	$ (7.3)	$ 53.8

CHANGES IN FINANCIAL POSITION

Canfor's ratio of current assets to current liabilities decreased to 1.7:1 at the end of 2002 from 2.0:1 at the end of 2001, mainly as a result of an increase in accounts payable and accrued liabilities. This increase is partly due to the accrual for termination benefits and mill closure costs discussed previously, but is also due to the fact that payables were unusually low at the end of 2001 as a result of deferring some of December's logging activities into January 2002.

Canfor's ratio of net debt to equity improved to a ratio of 41:59 from 43:57 in 2001. The improvement mainly resulted from the impact of the stronger Canadian dollar on US dollar denominated debt at the year end, as well as the scheduled debt repayments made during the year and the liability portion of the convertible debenture now being fully accounted for as equity.

The changes in the components of these ratios during 2002 are detailed in the Consolidated Cash Flow Statement of the Financial Statements. The more significant changes are discussed below.

Operating Activities

Cash generated from operating activities during 2002 was $25.6 million higher than the amount generated in 2001, even with the decrease in net income. The increase in cash from operations mainly resulted from changes in non-cash working capital items contributing $73.2 million of cash in 2002, whereas in 2001 changes in these items required $16.0 million of cash.

In 2002, the major changes in non-cash working capital were an increase in accounts payable and accrued liabilities of $58.9 million, as discussed above, a decrease in accounts receivable of $22.7 million, and an increase in inventories of $10.3 million. The $45.8 million reversal of countervailing and anti-dumping duties accrued in 2001 did not involve cash since these preliminary duties did not require cash payments to be made.

Financing Activities

In 2002, Canfor used $76.3 million for financing activities, including $49.9 million in long-term debt repayments. In 2001, Canfor issued $321.5 million (equivalent to US $220 million) in long-term debt, made $255.5 million in debt repayments, and received proceeds of $18.8 million on the closure of a cross-currency swap. In both 2002 and 2001, the Company paid quarterly cash dividends of $0.065 per common share, or $0.26 per common share for the year ($21.1 million in total) to its shareholders.

Investing Activities

Canfor increased its investment in capital assets by $13.8 million over the previous year. As a result of uncertainties in the marketplace and having just completed its mill modernization program in 2001, Canfor's capital program is primarily focused on maintaining operations, while conserving cash. Over the previous 3 years, Canfor spent over $179 million in strategic capital to modernize its mills. Of the $68.5 million invested in capital expenditures in 2002, $46.0 million, or approximately 40% of amortization, was spent on maintenance of business projects. The most significant projects included $15.0 million on roads and bridges and $10.6 million to replace the precipitator in the recovery boiler at the Prince George Pulp and Paper Mill. The balance of $22.5 million was invested in high return, low risk strategic projects that will either reduce costs or improve margins.

The majority of the proceeds from the sale of property, plant and equipment in 2002 arose from the sale of the former Eburne sawmill property, a portion of which was secured by a mortgage, which is due for repayment on or before May 2004.

As previously discussed under "Income Taxes", $60.2 million was paid to Howe Sound in 2001 as part of the restructuring of the business into a limited partnership. A further $5.0 million was paid to the Partnership in 2002.

Financial Requirements and Liquidity

At the end of 2002, Canfor had a cash position of $22.9 million and unused bank operating lines of credit of $164.2 million. At December 31, 2002, the amount of credit available under these operating lines has been reduced by $35.8 million of outstanding standby letters of credit. In early January 2003, these letters of credit were reduced by $22.0 million, which restored the amount available under the operating lines by an equivalent amount.

Provisions contained in Canfor's long-term borrowing agreements limit the amount of indebtedness that the Company can incur and the amount of dividends it may pay on its Common Shares. The amount of dividends the Company is permitted to pay under its long-term borrowing agreements is determined by reference to consolidated net earnings less certain restricted payments. As at December 31, 2002, the Company would be permitted under these agreements to incur $216.0 million of additional long-term debt (2001 – $135.2 million) and pay up to $68.7 million, or $0.85 per share, in dividends on its Common Shares (2001 – $79.1 million, or $0.98 per share). The agreements do not restrict payment of dividends on preferred shares or dividends paid in Common Shares of the Company.

For 2003, Canfor is planning capital expenditures of approximately $100 million, which includes $40 million on normal maintenance of business capital and $60 million on strategic capital. Strategic capital is targeted to either reduce costs or increase the value of the products that Canfor manufactures. Of the $60 million in planned strategic capital, $50 million has

been directed to the Wood Products segment. As part of the Cost Reduction/Margin Improvement Program announced in October 2002, $40 million of capital projects will be made in 2003 to upgrade the Fort St. John and Prince George sawmills. The upgrades will enable these mills to reduce costs while running 3 shifts. A further $10 million in margin improvement projects is planned for the Wood Products segment, mainly to install 6 linear wane optimizers, which will optimize grade mix and profitability by automating some of the decision-making at the sawmills. The remaining $10 million of strategic capital expenditures will be spent by the Pulp and Paper segment, mainly for projects related to energy reduction.

In 2003, $51.4 million is required for installment payments on long-term debt.

Canfor intends to finance its planned capital expenditures and scheduled debt repayments from cash generated from its operations.

RISKS AND UNCERTAINTIES

Most companies in the forest industry in North America, including Canfor, face similar business risks and uncertainties. In addition to the specific issues discussed above under each reporting segment, risks and uncertainties fall into the general business areas of markets, international commodity prices, currency exchange rates, environmental issues, forest land base, government regulations and, for Canadian companies, trade barriers and aboriginal land claims.

In order to address these risks and effectively manage them, Canfor's senior management is developing and articulating a vision for risk management and its interrelationship with Canfor's strategic plan. Accordingly, a corporate Risk Management position has been created, which reports to the Chief Financial Officer, with regular updates to the Audit Committee. This individual will work with corporate and operational management to identify, measure and prioritize the critical risks facing the Company, and to manage these risks by ensuring that they are adequately addressed through control and mitigating procedures and other management actions. The objectives of the risk management function include developing a common framework for understanding what constitutes principal business risks, ensuring that risk management activities are aligned with business strategies and planning activities, and providing effective governance in the area of risk management policies and programs. Initiatives currently underway include projects relating to hedging, credit risk, loss prevention, an insurance audit and a methodology for enterprise-wide risk management.

The Internal Audit function is contributing to this governance process by monitoring risk exposure, reviewing the risk management process, validating controls and other mitigating procedures, and giving assurance to senior management and the Audit Committee on management's assertions of residual risk exposure.

The future impact of the various uncertainties and potential risks described in the following paragraphs cannot be quantified or predicted. However, Canfor does not foresee unmanageable adverse effects on its operations, and believes that it is well positioned to deal with such matters as may arise.

Aboriginal Issues

In 1997, the Supreme Court of Canada, in the Delgamuukw decision, confirmed the continued existence of Aboriginal title and rights in areas of British Columbia, which are not covered by treaties. Accordingly, Aboriginal groups have claimed Aboriginal title and rights over substantial portions of British Columbia, including areas where Canfor's forest tenures are situated, creating uncertainty as to the status of competing property rights. The Federal and Provincial governments have been seeking to negotiate settlements with Aboriginal groups throughout British Columbia in order to resolve these land claims.

Recently, the British Columbia Court of Appeal extended to a publicly traded forest company the Crown's duty to consult with an Aboriginal group in the context of a renewal of a tree farm licence . In a subsequent case, the British Columbia Supreme Court found that the Crown must also consult Aboriginal groups prior to approving a change in the control of a company which holds a forest licence. The duty to consult is triggered when the Crown is preparing to make a decision that may infringe Aboriginal and treaty rights. At this time, the existence and extent of any legal obligation of tenure holders to separately consult with Aboriginal groups remains unclear. However, Canfor will continue to consult with Aboriginal groups and address legitimate concerns to foster good relationships and minimize risks to its tenures and operational plans and will continue to participate with the Province in its consultations with Aboriginal groups.

The issues surrounding Aboriginal title and rights are not likely to be resolved in the near future. However, Canfor is committed to working with Aboriginal groups and with the Province to facilitate resolutions of these issues. To date, there has not been any impact on Canfor and its tenures resulting from Aboriginal land claims and the continuing treaty negotiation and settlement process.

In 2002 the Government of British Columbia updated its Aboriginal Consultation Policy in an attempt to create more certainty for businesses and Aboriginal groups when decisions are made that could have an impact on Aboriginal interests. The policy creates implementation challenges for the Government of British Columbia. The impact on Canfor and its tenures, if any, remains unclear.

Canada/US Softwood Lumber Dispute

The Canada/US Softwood Lumber Agreement expired on March 31, 2001 without being renewed or replaced. On April 2, 2001, countervailing duty (CVD) and anti-dumping duty (ADD) petitions covering certain softwood lumber products from Canada were filed with the US Department of Commerce (DOC) and the US International Trade Commission (ITC) by certain US industry and trade groups.

On August 9, 2001, the DOC announced their belief that imports of softwood lumber from Canada are subsidized and imposed a preliminary CVD rate of 19.31% on sales from August 17, 2001 to December 15, 2001. At December 31, 2001, Canfor had accrued CVD of $40.9 million.

On October 31, 2001, the DOC announced their belief that Canfor had been dumping product into the US marketplace, which has caused injury or a threat of injury to the US industry. The company-specific ADD preliminary rate assigned to Canfor was 12.98% for products sold into the US market commencing November 6, 2001. At December 31, 2001, Canfor had accrued ADD of $6.5 million.

On May 16, 2002, the ITC published its final written determination on injury and stated that Canadian softwood lumber threatens material injury to the US industry. CVD at 18.79% was applied to all producers and ADD at 5.96% was applied specifically to Canfor. Cash deposits were required for shipments into the US, effective from the Final Order date of May 22, 2002. As a result of the ITC's ruling that Canadian lumber shipments only posed a threat of injury, in the second quarter of 2002 Canfor reversed all preliminary CVD and ADD accrued prior to May 22, 2002.

The final amount and effective date of CVD and ADD that may be assessed on Canadian softwood lumber exports to the US cannot be determined at this time and will depend on appeals of the final determinations to any reviewing courts, NAFTA or WTO panels.

The Company and other Canadian forest product companies, the Federal Government and Canadian provincial governments (Canadian Interests) categorically deny the US allegations and strongly disagree with the final countervailing and dumping determinations made by the ITC and DOC. Canadian Interests continue to aggressively defend the Canadian industry in this US trade dispute. Canadian Interests may appeal the decision of these administrative agencies to the appropriate courts, NAFTA panels and the WTO. Notwithstanding the final rates established in the investigations, the final liability for the assessment of CVD and ADD will not be determined until each annual administrative review process is complete, or another settlement of the dispute is achieved.

Environmental Certifications

In recent years, environmental groups have been lobbying consumers to purchase products that have been certified by an independent third party as having been derived from well-managed forests. Pressure from the environmental groups has resulted in retailers of wood products requesting that producers provide them with verification that the products are "environmentally friendly". Canfor has responded by implementing a comprehensive third-party environmental certification strategy for its forest operations.

Canfor attained the International Organization for Standardization (ISO) 14001 environmental management system certification for all of its forest operations in 1999. In 2002 Canfor re-certified all of its forest operations to the ISO 14001 standard for another 3-year term and received ISO 14001 certification of the environmental management system at its Rustad sawmill. In addition, Canfor has achieved certification under the Canadian Standards Association (CSA) standard for sustainable forest management (Sustainable Forest Management System Standard CAN/CSA Z809-96) for its Forest Management Agreement (FMA) area at Grande Prairie, Alberta and for its Tree Farm Licences (TFLs) at its Chetwynd, Englewood, and Prince George, British Columbia operations. In 2002 Canfor re-certified the Grande Prairie FMA and the Chetwynd and Englewood TFLs to the CSA standard.

In 2002, Canfor received certification of 3.18 million hectares of forest operations in the Prince George and Quesnel timber supply areas and 180,000 hectares in TFL 30, near Prince George, to the Sustainable Forestry Initiative® (SFI) standard. The SFI program, created by the American Forest & Paper Association, is an exacting standard of environmental principles, objectives and performance measures that integrates the perpetual growing and harvesting of trees with the protection of wildlife, plants, soil and water quality, and a wide range of other conservation goals. This is the first SFI certification for Canfor, and the largest, by area, in Canada. With the addition of the SFI certification, Canfor now has 63% of its tenure area governed by certified Sustainable Forest Management (SFM) plans, and is committed to having SFM certification in place for all of its tenures.

Environmental Issues

Bill C-5, The Species at Risk Act (Canada) received Royal Assent in December 2002, but has not yet been proclaimed. The purpose of the Act is first to prevent wildlife species from becoming extinct, and second to provide for the recovery of species at risk. The Government of Canada will develop the regulations required under the Act prior to its coming into force by an Order in Council in 2003. The economic implications of this Act are potential reductions in timber harvests and increases in harvesting costs in British Columbia and Alberta, none of which can be predicted with certainty at this time.

In December 2002 the Government of Canada ratified the Kyoto Agreement. The Climate Change Plan for Canada indicates that federal and provincial energy and environment ministers endorsed the principle that companies that take early action should not be disadvantaged by an output-based emissions regime. Canfor was an early signatory to the Voluntary Climate Registry, a federal program introduced in 1994 to encourage companies to inventory and track their greenhouse gas emissions (GHGs) and take actions to stabilize and reduce those emissions. As of 2001, Canfor has reduced GHGs by more than 8% from 1990 levels, compared with the Canada Kyoto reduction commitment of 6%. It is unclear at present whether companies such as Canfor, that have taken early action to reduce GHGs, will be given full and fair credit for those actions. Under the federal Climate Change Plan, the pulp and paper sector and other key industry sectors will be negotiating sectoral covenants with the federal government. The outcome of these negotiations will determine what further GHG reductions may be required.

Under a regulation passed by the previous provincial government in 1992, pulp mills in British Columbia using chlorine compounds for pulp bleaching were required to eliminate organochlorine discharge (measured as AOX) in their effluent by the end of 2002. An Order in Council was signed in July 2002 eliminating the zero AOX requirement and replacing the monthly limit of 1.5 kg/Adt with a limit of 0.6 kg/Adt. All of Canfor's pulp mills are able to comply with the new monthly AOX limit.

Canada-wide standards have been established by the Government of Canada for respirable particulate (PM 2.5) and ozone levels in the ambient air. The standard will be effective in 2010 following additional technical, scientific and economic analysis required to be completed by the end of 2005. The PM 2.5 standard could require future source reductions of particulate emissions from Canfor's pulp, paper and sawmill facilities, the cost of which cannot yet be determined.

Financial Market Risk

Demand for forest products, both pulp and paper and wood products, is closely related to global business conditions and tends to be cyclical in nature. Product prices can be subject to volatile change. Canfor, like the majority of the Canadian forest products industry, competes in a global market and the majority of its products are sold in US dollars. Consequently, foreign currency relationships pose a significant uncertainty. Shifts in these relationships can have a major impact, positive or negative, on profits from operations. A weakening Canadian dollar relative to the US dollar has operating benefits to the Company. By maintaining a substantial proportion of its debt in US dollars, Canfor has partially mitigated the impact of currency fluctuations in that currency. The sensitivity of Canfor's results to currency swings and prices for its principal products is discussed at the end of this section.

Since Canfor's long-term debt is primarily fixed in rate, there is no significant impact to net income when interest rates change. Canfor, from time to time, uses derivative markets to hedge future movements of exchange rates or commodity prices. As at year end, Canfor had forward exchange contracts totaling US $140 million outstanding, at an average rate of US $0.623, which will be exercised at various dates throughout 2003. These contracts have been designated as a hedge against future US dollar revenues, and, therefore, any gain or loss realized when the contracts are exercised will be recognized in income when the related hedged revenue is recorded.

Labour Agreements

In December 2002, Canfor negotiated an early renewal of the labour agreement with the PPWC (Pulp, Paper and Woodworkers of Canada) Local 9, covering all hourly workers, except for the paper machine crew, at the Prince George Pulp and Paper Mill. The renewed contract is for a five-year term, expiring April 30, 2008.

The labour agreement with the IWA (Industrial, Wood and Allied Workers of Canada) covering all of their BC certified operations expires in June 2003. Labour agreements with the CEP (Communications, Energy and Paperworkers Union) expire in April 2003 for the Northwood pulp mill and the paper machine crew at the Prince George Pulp and Paper Mill and in June 2003 for the Taylor sawmill.

Provincial Forest Policy Reform

On December 17, 2002, the Forest Statutes Amendment Act (No. 2), 2002 was proclaimed into force. This legislation effects a number of significant changes to the Forest Act and the Forest Practices Code. These changes are intended to reduce the regulatory burden that has resulted from the implementation of the Code in 1995. It is hoped that the changes will reduce transactional and operational costs, balance social, environmental and economic interests, and shift the emphasis from a prescriptive, planning-based regime to a results-based forest and range practices regime. The changes to the Act and Code also include an increase in the maximum penalties for certain contraventions, but introduce a due diligence defence to allow licencees to demonstrate they took all reasonable care to avoid a contravention.

The new legislation provides for a 2-year transition period leading to a new Forest and Range Practices Act, which will be fully implemented between April 2003 and April 2005.

The full extent of the impact of these reforms is presently unknown until regulations are enacted under the new Act during 2003.

The Government of British Columbia continues to explore possible changes to the province's stumpage system so that it better reflects market price fluctuations. The government is approaching these changes through 2 separate reviews — one for the coast and one for the interior of the province. It is hoped that these reviews will result in a remedy for the regional inequities that exist in the current stumpage system.

Legal Claims

The Woodworkers for Fair Forest Policy Society and an individual have filed a petition against the Minister of Forests seeking a judicial review of various issues in connection with Canfor's TFL 37 (Englewood) and, among other things, the cancellation of the TFL. The action results from the closure of the Eburne sawmill in 1998. Canfor was added as a party to the proceedings, which were heard in October 2000. The Supreme Court of British Columbia dismissed the claims of the petitioners with costs, but the petitioners filed a notice of appeal to the Court of Appeal. This appeal was dismissed in 2002.

NAFTA Lawsuit

On July 11, 2002, Canfor filed a Notice of Arbitration and Statement of Claim against the Government of the United States for damages under the North American Free Trade Agreement (NAFTA) as a result of the US Department of Commerce's (DOC) preliminary and final determinations in the countervailing and anti-dumping proceedings. Canfor has asserted that the actions of the US Government have amounted to breaches of certain provisions of NAFTA, including the failure to provide Canfor with fair and equitable treatment in accordance with international law.

The Statement of Claim seeks damages for not less than US $250 million resulting from the actions of the US government in issuing the preliminary and final countervailing duty (CVD) and anti-dumping duty (ADD) against Canfor. Canfor believes that the DOC has been arbitrary, discriminatory and capricious in making the preliminary and final CVD and ADD determinations.

The next step is for an independent tribunal to be struck to hear Canfor's claim, which was to be done within 90 days of filing the Claim. Canfor and the US Government each have the right to select one member of the tribunal, and the third member will be appointed by the agreement of Canfor and the US Government. If the parties cannot agree, the World Bank will make the third selection. On October 8, 2002, Canfor named former New Brunswick Premier, Frank McKenna, as its representative on the NAFTA tribunal. The US has challenged Mr. McKenna's appointment, however, Canfor has advised the US that it will defend this appointment. The US has appointed Conrad Harper, a lawyer with the firm of Simpson, Thacher & Bartlett, New York.

SENSITIVITIES

The sensitivity of Canfor's results to changes in its product prices while operating at full capacity, expressed in terms of after-tax earnings, is estimated to be approximately as follows:

(millions of dollars)	
Lumber – US $10 change per Mfbm	$ 26.5
Pulp – US $10 change per tonne	12.2
Specialty Kraft Paper – US $10 change per tonne	1.6
Canadian dollar – US $0.01 change per Canadian dollar	13.2

DEFINITIONS OF SELECTED FINANCIAL TERMS

Book Value per Share is the shareholders' equity, including the equity component of the convertible subordinated debentures, at the end of the year, divided by the number of common shares outstanding at the end of the year plus the number of common shares exchangeable for the convertible subordinated debentures.

Capital Employed consists of the funds invested or retained in Canfor in the form of shares or liabilities. It is composed of unpresented cheques, current bank loans (net of cash and temporary investments), current portion of long-term debt, long-term debt, future income taxes arising from timing differences and shareholders' equity. Long-term liabilities and other accruals such as deferred reforestation costs, unfunded pension and post employment benefits, countervailing and anti-dumping duty provisions and unrealized foreign exchange losses on long-term debt are specifically excluded because they do not represent borrowed funds or funds invested by shareholders.

Earnings Before Interest, Taxes and Amortization (EBITDA) represents operating income plus amortization.

Net Debt is total debt less cash and temporary investments.

Net Income per Common Share is calculated as described in Note 20 to the Consolidated Financial Statements.

Return on Assets is equal to net income plus interest, after tax, divided by the average of the total assets at the beginning and end of the year.

Return on Capital Employed is equal to net income plus interest, after tax, divided by the average of the capital employed during of the year.

Return on Common Shareholders' Equity is equal to net income for the year, divided by the average of total shareholders' equity at the beginning and end of the year.

Management's Responsibility

The information and representations in this Annual Report are the responsibility of management and have been approved by the Board of Directors. The consolidated financial statements were prepared by management in accordance with accounting principles generally accepted in Canada and, where necessary, reflect management's best estimates and judgments at this time. It is reasonably possible that circumstances may arise which cause actual results to differ. Management does not believe it is likely that any differences will be material. The financial information presented throughout this report is consistent with that contained in the consolidated financial statements.

Canfor maintains systems of internal accounting controls, policies and procedures to provide reasonable assurances as to the reliability of the financial records and the safeguarding of its assets. The Internal Audit Department performs independent reviews of the accounting records and related procedures. The Internal Audit Department reports its findings and recommendations both to management and the Audit Committee.

The Board of Directors is responsible for ensuring that management fulfills its responsibilities for financial reporting and is ultimately responsible for reviewing and approving the financial statements and Management's Discussion and Analysis. The Board carries out these activities primarily through its Audit Committee.

The Audit Committee is comprised of 4 Directors who are not employees of the company. The Committee meets periodically throughout the year with management, external auditors and internal auditors to review their respective responsibilities, results of the reviews of internal accounting controls, policies and procedures and financial reporting matters. The external and internal auditors meet separately with the Audit Committee.

The consolidated financial statements and Management's Discussion and Analysis have been reviewed by the Audit Committee, which recommended their approval by the Board of Directors. The consolidated financial statements have been audited by PricewaterhouseCoopers LLP, the external auditors, whose report follows.

February 13, 2003

David Emerson

David L. Emerson
President and
Chief Executive Officer

Charles Reid

Charles W. Reid
Group Vice-President,
Finance and Chief Financial Officer

Auditors' Report

To the Shareholders of Canfor Corporation

We have audited the consolidated balance sheets of Canfor Corporation as at December 31, 2002 and December 31, 2001, and the consolidated statements of income and retained earnings and cash flow for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2002 and December 31, 2001, and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles. As required by the *British Columbia Company Act*, we report that, in our opinion, these principles have been applied on a basis consistent with that of the preceding year.

PricewaterhouseCoopers LLP

February 13, 2003
Chartered Accountants
Vancouver, B.C.

Consolidated Statements of Income and Retained Earnings

Year ended December 31 (millions of dollars)	2002	2001
Net sales	$ 2,112.3	$ 1,985.7
Costs and expenses		
Manufacturing and product costs	1,889.8	1,757.6
Amortization	115.1	106.0
Selling and administration	65.0	59.6
	2,069.9	1,923.2
Reversal of duties accrued in prior year (Note 12)	45.8	–
Termination benefits and mill closure costs (Note 23)	(33.1)	–
Operating income	55.1	62.5
Equity income of affiliated companies (Note 3)	5.0	1.1
Interest expense (Note 13)	(59.2)	(64.2)
Other income (expense)	9.0	(0.3)
Unusual items (Note 17)	–	8.5
Income before income taxes	9.9	7.6
Income tax recovery (Note 15)	1.6	18.8
Net income	$ 11.5	$ 26.4
Net income per common share (in dollars) (Note 20)		
- Basic	$ 0.07	$ 0.27
- Diluted	$ 0.07	$ 0.27
Retained earnings, beginning of year	$ 151.9	$ 151.4
Net income for the year	11.5	26.4
Common share dividends	(21.1)	(21.1)
Interest on equity component of convertible subordinated debentures, net of income taxes (Note 8)	(5.6)	(4.8)
Retained earnings, end of year	$ 136.7	$ 151.9

Year ended December 31 (millions of dollars)	2002	2001
Cash generated from (used in)		
Operating activities		
Net income	$ 11.5	$ 26.4
Items not affecting cash:		
Amortization	115.1	106.0
Reversal of accrued duties (Note 12)	(45.8)	–
Gain on disposal of assets	(11.7)	(1.5)
Income taxes	(3.5)	(19.7)
Other	5.6	23.6
	71.2	134.8
Change in non-cash working capital (Note 21)	73.2	(16.0)
	144.4	118.8
Financing activities		
Proceeds from long-term debt	–	321.5
Repayment of term bank loan (Note 6)	–	(175.4)
Repayment of long-term debt	(49.9)	(50.1)
Repayment of acquisition bank loan (Note 6)	–	(30.0)
Proceeds on settlement of cross-currency swap (Note 18)	–	18.8
Dividends paid to common shareholders	(21.1)	(21.1)
Interest on convertible subordinated debentures, net of income taxes	(5.5)	(4.3)
Other	0.2	(2.7)
	(76.3)	56.7
Investing activities		
Howe Sound Pulp and Paper Limited Partnership (Note 19)	(5.0)	(60.2)
Purchase of property, plant, equipment and timber	(68.5)	(54.7)
Proceeds from sale of property, plant and equipment	21.7	3.5
Mortgage receivable on sale of property (Note 3)	(15.7)	–
Other	(7.9)	(10.3)
	(75.4)	(121.7)
Increase (decrease) in net cash (short-term indebtedness)	(7.3)	53.8
Net cash (short-term indebtedness) at beginning of year	30.2	(23.6)
Net cash at end of year	$ 22.9	$ 30.2
Net cash comprises		
Cash	$ 18.4	$ 8.3
Temporary investments	4.5	24.0
Operating bank loans	–	(2.1)
	$ 22.9	$ 30.2

Interest paid in 2002 was $63.5 million (2001 – $61.6 million) and income taxes paid were $2.1 million (2001 – $5.8 million recovered).

Consolidated Balance Sheets

As at December 31 (millions of dollars)	2002	2001
Assets		
Current assets		
Cash	$ 18.4	$ 8.3
Temporary investments	4.5	24.0
Accounts receivable		
Trade	148.9	176.3
Other	29.7	24.9
Future income taxes (Note 15)	25.4	13.2
Inventories (Note 2)	422.2	411.9
Prepaid expenses	20.7	20.0
Total current assets	669.8	678.6
Long-term investments and other (Note 3)	94.7	71.3
Property, plant, equipment and timber (Note 4)	1,424.2	1,469.0
Deferred charges (Note 5)	139.3	159.9
	$ 2,328.0	$ 2,378.8

APPROVED BY THE BOARD

R. Laird Cliff

Director, R.L. Cliff

David Emerson

Director, D.L. Emerson

As at December 31 (millions of dollars)	2002	2001
Liabilities		
Current liabilities		
Operating bank loans (Note 6)	$ –	$ 2.1
Accounts payable and accrued liabilities	300.6	244.3
Current portion of long-term debt (Note 7.1)	51.4	52.7
Current portion of deferred reforestation	38.8	33.9
Income taxes payable	5.8	1.2
Total current liabilities	396.6	334.2
Long-term debt		
Long-term debt (Note 7.1)	643.4	706.5
Convertible subordinated debentures – liability component (Note 8)	–	8.2
Total long-term debt	643.4	714.7
Other accruals and provisions (Note 9)	83.9	118.4
Future income taxes, net (Note 15)	154.5	147.0
Deferred credit (Note 19)	95.7	104.0
Shareholders' Equity		
Share capital (Note 10)	658.3	657.7
Convertible subordinated debentures – equity component (Note 8)	155.0	146.8
Retained earnings	136.7	151.9
Foreign exchange translation adjustment	3.9	4.1
	953.9	960.5
Commitments and contingencies (Note 22)		
	$ 2,328.0	$ 2,378.8

Statements of Segmented Information

(millions of dollars)	Wood Products	Pulp Products	Pulp and Specialty Kraft Paper	Coastal Operations	Corporate and Other	Consolidated
Year ended December 31, 2002						
Net sales to external customers (Note a)	**$ 1,348.1**	**466.6**	**175.0**	**122.6**	**–**	**$ 2,112.3**
Net sales to other segments (Note b)	**$ 88.0**	**–**	**–**	**16.9**	**–**	**$ 104.9**
Operating income (loss)	**$ 70.8**	**19.2**	**(6.5)**	**5.7**	**(34.1)**	**$ 55.1**
Amortization	**$ 49.9**	**35.6**	**14.7**	**7.9**	**7.0**	**$ 115.1**
Capital expenditures	**$ 35.4**	**9.1**	**13.7**	**6.4**	**3.9**	**$ 68.5**
Identifiable assets (Note c)	**$ 975.7**	**699.2**	**177.3**	**69.6**	**406.2**	**$ 2,328.0**
Year ended December 31, 2001						
Net sales to external customers (Note a)	$ 1,192.1	499.5	177.2	116.9	–	$ 1,985.7
Net sales to other segments (Note b)	$ 83.2	–	–	9.8	–	$ 93.0
Operating income (loss)	$ 74.9	31.4	(7.3)	(6.8)	(29.7)	$ 62.5
Amortization	$ 42.2	35.3	14.2	9.2	5.1	$ 106.0
Capital expenditures	$ 17.8	11.8	14.7	7.2	3.2	$ 54.7
Identifiable assets (Note c)	$ 995.3	717.0	182.2	67.7	416.6	$ 2,378.8

Year ended December 31 (millions of dollars)	2002	2001
Sales by location of customer		
Canada	**$ 421.0**	$ 420.6
United States	**1,204.0**	1,085.7
Europe	**207.7**	224.5
Far East and other	**279.6**	254.9
	$ 2,112.3	$ 1,985.7

(a) No single customer accounted for 10% or more of the Company's total sales.
(b) Sales to other segments are accounted for at prices which approximate market.
(c) Substantially all of the Company's property, plant, equipment and timber is located in Canada.

1. Significant Accounting Policies

Basis of Presentation of Financial Statements

These financial statements include the accounts of Canfor Corporation (the Company) and its subsidiary companies, hereinafter referred to as "Canfor". Equity investments are accounted for by recording the original investment at cost and subsequently adjusting for the Company's share of post acquisition earnings.

Use of Estimates

The preparation of financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. It is reasonably possible that circumstances may arise which cause actual results to differ from management estimates, however, management does not believe it is likely that such differences will materially affect Canfor's financial position.

Significant areas requiring the use of management estimates are deferred reforestation costs, inventory valuations, amortization rates and pension and other benefit plan assumptions.

Temporary Investments

Temporary investments comprise bankers acceptances, commercial paper and other short-term instruments and are valued at cost, which approximates fair value.

Valuation of Inventories

Inventories of wood products, pulp and kraft paper are valued at the lower of average cost and net realizable value. Logs and chips are valued at average cost or the greater of net realizable value and replacement cost if lower than average cost. Processing materials and supplies are valued at the lower of average cost and replacement cost.

Property, Plant, Equipment and Timber

Canfor capitalizes the costs of major replacements, extensions and improvements to plant and equipment, together with related interest incurred during the construction period on major projects.

Assets are amortized over the following estimated productive lives:

Buildings	10 to 50 years
Mobile equipment	3 to 20 years
Pulp and kraft paper machinery and equipment	20 years
Sawmill machinery and equipment	5 to 12 years
Logging machinery and equipment	4 to 20 years
Logging roads and bridges	5 to 20 years
Other machinery and equipment	3 to 20 years

Amortization of logging and manufacturing assets is calculated on a unit of production basis.

Amortization of plant and equipment not employed in logging and manufacturing is calculated on a straight-line basis.

Amortization of logging roads and timber is calculated on a basis related to the volume of timber harvested.

Deferred Charges

Software development costs relating to major systems are deferred and amortized over periods not longer than 10 years.

Deferred Reforestation

Canfor accrues the undiscounted cost of the reforestation required under its timber harvest agreements at the time that the timber is harvested.

Employee Benefit Plans

Canfor has various defined benefit plans providing both pension and other retirement benefits to most of its salaried employees and certain hourly employees not covered by forest industry-union plans. Canfor also provides certain health care benefits and pension bridging benefits to eligible retired employees.

Canfor accrues the costs and related obligations of the pension and other retirement benefit plans using the projected benefit actuarial method prorated on service and management's best estimates of expected plan investment performance, salary escalation, and other relevant factors. The difference between costs of employee benefits charged against earnings and Canfor's contributions to the plans, which are made in accordance with actuarial recommendations and pension commission regulations, is included in prepaid pension benefits or post-employment benefits on the balance sheet.

For hourly employees covered by forest industry-union defined benefit pension plans, earnings are charged with Canfor's contributions required under the collective agreements.

Revenue Recognition

Canfor's revenues are derived from 4 major product lines: softwood lumber, pulp, kraft paper and raw logs. Revenue is also derived from other products, including chips, plywood, panels, refined fibre and fibremat, and from commissions on pulp, logs and chips. Revenue is recognized when the significant risks and rewards of ownership are transferred, which is generally at the time of shipment. In the case of lumber sales that are made through distribution centres, revenue is recognized when the product is shipped from the mill. Canfor retains the risk of loss in transit until the product is shipped out of the distribution centre, but is fully insured for any potential losses.

Foreign Currency

Effective January 1, 2002, the Canadian Institute of Chartered Accountants amended its accounting policy for foreign currency translation to eliminate the deferral and amortization method of accounting for unrealized translation gains and losses on long-term monetary assets and liabilities. As permitted by the revised policy, Canfor continues to hedge its US dollar long-term debt, as discussed below, and, therefore, no change in accounting for the unrealized translation loss on its long-term debt was required.

The majority of Canfor's sales and long-term debt are denominated in foreign currencies. Foreign currencies are translated into Canadian dollars using the temporal method as follows:

- Monetary assets and liabilities at year-end or applicable hedged exchange rates; non-monetary assets and liabilities at historical rates; revenues and expenses at exchange rates prevailing at the time the transaction occurs.
- Exchange gains or losses are reflected in income immediately, with the exception of unrealized translation gains or losses related to Canfor's US dollar long-term debt, which are hedged with future revenue streams. Any exchange gains or losses on US dollar long-term debt are deferred and recognized as an adjustment of the related revenues at the time that the debt is repaid.

Canfor's foreign operations are considered to be self-sustaining and the assets and liabilities are translated using the current rate method. The translation gain or loss is included as a component of shareholders' equity.

Income Taxes

Canfor accounts for income taxes using the liability method. Under this method, future income tax assets and liabilities are determined based on the temporary differences between the accounting basis and the tax basis of assets and liabilities. These temporary differences are measured using the current tax rates and laws expected to apply when these differences reverse. Future tax benefits, such as capital loss carry-forwards, are recognized to the extent that realization of such benefits is considered more likely than not. The effect on future tax assets and liabilities of a change in income tax rates is recognized in earnings in the period that the substantive enactment date of the change occurs.

Derivative Financial Instruments

Derivative financial instruments are utilized by Canfor to manage risk, including the foreign currency risk on its US dollar denominated sales. For example, Canfor purchases foreign exchange forward contracts to hedge anticipated sales to customers in the United States and the related accounts receivable. Canfor's policy is not to utilize derivative financial instruments for trading or speculative purposes.

Canfor formally documents all relationships between hedging instruments and hedged items, as well as its risk management objective and strategy for undertaking various hedge transactions. This process includes linking all derivatives to specific assets and liabilities or to specific firm commitments or forecasted transactions. Canfor also formally assesses, both at the hedge's inception and on an ongoing basis, whether the derivatives that are used in hedging transactions are effective in offsetting changes in fair values or cash flows of hedged items.

Gains and losses on forward foreign exchange contracts used to hedge US dollar denominated sales are recognized as an adjustment to revenues at the time that the contract is exercised.

Stock-based Compensation Plans

Canfor has 3 stock-based compensation plans. No compensation expense is recognized when stock options are issued to employees under the Stock Option Performance Plan. Any cash consideration received from employees when they exercise the options is credited to share capital. Compensation expense is recognized for Canfor's contributions to the Employee Share Purchase Plan and the Deferred Share Unit Plan.

2. Inventories

(millions of dollars)	2002	2001
Wood products, pulp and kraft paper	$ 253.5	$ 215.9
Logs and chips	101.3	127.3
Processing materials and supplies	67.4	68.7
	$ 422.2	$ 411.9

3. Long-term Investments and Other

(millions of dollars)	2002	2001
Investment in 317231 British Columbia Ltd.[(a)]		
Cost of common shares	$ 45.1	$ 45.1
Accumulated equity income	3.3	1.2
Preferred shares		
Seaboard Shipping Company Limited [(b)]	9.8	11.4
Other investments	5.4	3.5
Mortgage receivable from sale of property [(c)]	16.6	–
Other deposits and loans	14.5	10.1
	$ 94.7	$ 71.3

(a) Through its investment in 317231 British Columbia Ltd., the Company owns a one-third interest in Lakeland Mills Ltd. and The Pas Lumber Company Ltd., which own sawmills in the Prince George, British Columbia region (Note 22). The combined assets and liabilities of the 2 mills are $138.3 million (2001 – $125.8 million) and $75.4 million (2001 – $72.0 million), respectively.

(b) During the year, Seaboard Shipping Company Limited issued further preferred shares in the amount of $0.9 million (2001 – $1.0 million), and subsequently redeemed preferred shares in the amount of $2.5 million (2001 – $1.1 million).

(c) Relates to the sale of the former site of the Eburne sawmill, which was closed in 1998. Proceeds are secured by a mortgage, which becomes due on or before May 15, 2004.

4. Property, Plant, Equipment and Timber

December 31, 2002 (millions of dollars)	Cost	Accumulated Amortization	Net Book Value
Land	$ 12.7	$ –	$ 12.7
Pulp and kraft paper mills	1,134.6	500.9	633.7
Wood products mills	520.0	319.2	200.8
Logging buildings and equipment	65.4	54.0	11.4
Logging roads and bridges	245.7	174.5	71.2
Other equipment and facilities	127.9	69.2	58.7
Timber	481.7	46.0	435.7
	$ 2,588.0	$ 1,163.8	$ 1,424.2

Included in the above are assets under construction in the amount of $18.3 million (2001 – $10.3 million), which are not being amortized.

December 31, 2001 (millions of dollars)	Cost	Accumulated Amortization	Net Book Value
Land	$ 14.4	$ –	$ 14.4
Pulp and kraft paper mills	1,114.9	456.0	658.9
Wood products mills	505.1	290.9	214.2
Logging buildings and equipment	65.0	52.6	12.4
Logging roads and bridges	231.7	162.5	69.2
Other equipment and facilities	120.2	61.8	58.4
Timber	481.7	40.2	441.5
	$ 2,533.0	$ 1,064.0	$ 1,469.0

5. Deferred Charges

(millions of dollars)	2002	2001
Prepaid pension benefits (Note 14)	$ 70.6	$ 69.6
Unrealized foreign exchange loss on long-term debt	52.9	74.0
Software development costs	14.3	14.3
Debt issue and other expenses	1.5	2.0
	$ 139.3	$ 159.9

Deferred charges expensed during the year amounted to $13.4 million (2001 – $10.7 million), including a foreign exchange loss of $6.9 million realized on the repayment of US dollar long-term debt (2001 – $7.2 million).

6. Bank Loans

In 2001, Canfor repaid its term and acquisition bank loans, which were used to finance the acquisition of Northwood Inc. in 1999.

Canfor had $164.2 million of unused bank operating lines of credit as of December 31, 2002 (2001 – $197.9 million). The amount of credit available under these lines of credit has been reduced by $35.8 million, which represents standby letters of credit outstanding as of December 31, 2002.

7. Long-term Debt

7.1 Summary of Long-term Debt

(millions of dollars)	2002	2001
Privately placed senior notes		
US $20 million (2001 – US $40 million), interest at 7.75%, repayable in 5 equal annual instalments commencing June 1, 1999	$ 31.4	$ 63.8
US $25 million (2001 – US $37.5 million), interest at 7.73%, repayable in 4 equal annual instalments commencing June 28, 2001	39.2	59.8
US $125 million, interest at 8.24%, repayable in 4 equal annual instalments commencing September 1, 2004	196.1	199.4
US $50 million, interest at 6.82%, repayable in 5 equal semi-annual instalments commencing April 1, 2005	78.4	79.8
US $30 million, interest at 7.64%, repayable March 14, 2006	47.1	47.9
US $33 million, interest at 7.74%, repayable March 1, 2007	51.8	52.7
US $15 million, interest at 7.88%, repayable March 1, 2008	23.5	23.9
US $45 million, interest at 7.98%, repayable March 1, 2009	70.6	71.8
US $97 million, interest at 8.03%, repayable in 3 equal annual instalments commencing March 1, 2009	152.1	154.8
Other long-term obligations	4.6	5.3
	694.8	759.2
Less current portion	51.4	52.7
	$ 643.4	$ 706.5

The agreements relative to the privately placed senior notes contain provisions limiting the amount of indebtedness that the Company and its designated subsidiaries can incur and the amount of dividends payable on its common shares. Under these agreements, the Company and its designated subsidiaries can presently incur $216.0 million additional long-term debt (at December 31, 2001 – $135.2 million additional long-term debt could be incurred) and pay up to $68.7 million or $0.85 per share in dividends on its Common Shares (2001 – dividends up to $79.1 million or $0.98 per share could be paid).

7.2 Fair Value

The fair value of long-term debt at December 31, 2002 was $748.3 million (2001 – $774.0 million).

7.3 Debt Repayments

Long-term debt repayments for the next 5 years are as follows:

(millions of dollars)	
2003	$ 51.4
2004	68.9
2005	80.8
2006	127.4
2007	116.5

8. Convertible Subordinated Debentures

On November 23, 1999, the Company issued $155.0 million of unsecured convertible subordinated debentures as part of the purchase price payable by the Company for all the outstanding shares of Northwood Inc. The debentures bear interest at 6.25% per annum, payable semi-annually, and mature on November 23, 2006. The debentures are convertible, at the holder's option, into common shares of the Company at a conversion price of $13.20 per share. Upon a change of control of the Company, each holder may require the Company to purchase the holder's debentures at 100% of principal plus accrued and unpaid interest. The debentures are redeemable after November 23, 2002, at the option of the Company, at 100% of principal plus accrued and unpaid interest, provided that from the third year to the fifth year the debentures may only be redeemed if the weighted average closing price of the Company's common shares for the 20 consecutive trading days ending 5 days prior to the date on which notice of redemption is given exceeds 120% of the conversion price. The Company has the option to satisfy its obligation to pay any portion of the applicable principal and interest, or redemption or purchase price, by delivery of shares to the trustee and subsequent sale of such shares and delivery to the holders of cash equal to the principal and interest, or redemption or purchase price, of the debentures.

The convertible subordinated debentures are being accounted for in accordance with their substance and were initially presented in the financial statements in their component parts, measured at their respective fair values at the time of issue. The liability component in 2001 represented the remaining net present value of the outstanding interest payments to November 23, 2002, the first date that the Company had the option to retire the debentures through the issue of shares. By November 23, 2002, the equity component of the debentures had increased to the full face value by charges to retained earnings and a corresponding reduction in interest expense.

In computing basic earnings per share, the charges to retained earnings are deducted from net earnings to arrive at net earnings attributable to common shareholders.

The fair value of the convertible subordinated debentures at December 31, 2002 was $150.5 million (2001 – $155.7 million).

9. Other Accruals and Provisions

(millions of dollars)	2002	2001
Countervailing and anti-dumping duty provision (Note 12)	$ –	$ 47.4
Deferred reforestation	42.3	42.3
Post-employment benefits (Note 14)	26.1	23.0
Other long-term liabilities	15.5	5.7
	$ 83.9	$ 118.4

10. Share Capital

Authorized

10,000,000 preferred shares, with a par value of $25 each
1,000,000,000 common shares without par value

(millions of dollars)	2002	2001
Issued		
81,156,010 common shares (2001 – 81,088,847)	$ 658.3	$ 657.7

During 2002, the Company issued 67,163 common shares in connection with its stock option plans, as discussed in Note 11.

11. Stock-based Compensation

The Company has 3 stock-based compensation plans, which are described below.

Stock Option Performance Plan

The Company has a stock option performance plan pursuant to which stock options are granted to selected officers and senior managers. The stock option performance plan provides for the issuance of up to a maximum of 5.8 million common shares at an exercise price equal to the market price of the Company's common shares on the date of grant. However, there are various criteria that limit the amount of options exercisable during each option year within the option period. A summary of the status of the plan as of December 31, 2002 and 2001, and changes during the years ending on those dates is presented below:

	2002		2001	
	Shares	Weighted Average Exercise Price	Shares	Weighted Average Exercise Price
Outstanding at the beginning of the year	4,886,850	$ 10.93	4,023,600	$ 11.58
Granted	737,500	9.78	908,250	8.34
Exercised	(67,163)	8.58	(5,000)	7.30
Cancelled	(21,000)	12.30	(40,000)	17.64
Outstanding at the end of the year	5,536,187	$ 10.80	4,886,850	$ 10.93

The following table summarizes information about stock options outstanding at December 31, 2002:

	Options Outstanding				Options Exercisable	
Range of Exercise Prices	Options Outstanding	Weighted Average Remaining Life (Years)	Weighted Average Exercise Price		Options Exercisable	Weighted Average Exercise Price
$7.30 to $7.57	97,000	1.7	$ 7.32		–	$ –
$8.30 to $8.66	964,587	7.7	8.34		370,087	8.40
$9.25 to $11.80	3,124,600	2.5	9.39		566,183	9.27
$15.80	1,220,000	0.4	15.80		–	–
$18.75	130,000	0.4	18.75		–	–
	5,536,187		$ 10.80		936,270	$ 8.92

Employee Share Purchase Plan (ESOP)

Canfor has a share purchase plan, which is available to all employees. Purchases of common shares under this plan occur on the open market. Under the plan the employees can purchase up to 10% of their base salary or wage. Canfor matches 30% of the first 5% of the amount contributed by the employee and pays the share purchase plan brokerage fees. In 2002, contributions of $1.2 million were made towards the purchase of the Company's common shares under the terms of the ESOP (2001 – $1.1 million).

Deferred Share Unit Plan

On January 1, 2002, the Company implemented a Deferred Share Unit Plan for non-employee directors of the Company. A Deferred Share Unit (DSU) is a right granted to a non-employee director to receive one common share of the Company, purchased on the open market, or the cash equivalent, on a deferred payment basis. The maximum number of DSUs outstanding under the plan is 1,000,000, and currently each non-employee director is entitled to 2,500 DSUs per year. The value of the DSUs, when redeemed, is equal to the market value of the shares on the redemption date, including the value of dividends paid on the Company's common shares, if any, as if they had been reinvested in additional DSUs on each payment date. The DSUs may only be redeemed upon a Director's retirement from the Company, its subsidiaries or any affiliated entity. The value of the outstanding DSUs at December 31, 2002 was $0.2 million.

Pro-forma Disclosure

During 2002, Canfor granted a total of 737,500 stock options to employees at exercise prices ranging from $7.57 to $10.10, which were the market prices on the dates the options were granted. One third of the options are exercisable after each of the first, second and third years and the options expire in 2012.

Canadian generally accepted accounting principles encourage, but do not require, application of a fair value based method of accounting for the type of stock options described above. Under this method, the fair value of a stock option is determined using an option pricing model that takes into account, as of the grant date, the exercise price, the expected life of the option, the current price of the underlying stock, its expected volatility, expected dividends on the stock, and the risk-free interest rate over the expected life of the option.

As permitted by Canadian generally accepted accounting principles, Canfor has elected not to use the fair value based method of accounting for stock options because of its limited use of stock-based compensation. Accordingly, no compensation expense was recorded at the time that the above options were granted. Had compensation cost been determined based on the fair value at the grant date consistent with the fair value based method of accounting, the resulting after-tax compensation cost for options granted after January 1, 2002 would have amounted to approximately $2.3 million. This amount would have been recognized over 3 years, which is the period of service during which the options will be earned by the employees. The after-tax impact on the current year would have been to reduce net income by $1.3 million and to decrease basic and diluted earnings per share by $0.02.

The fair value of the stock options granted in 2002 was estimated on each grant date using a Black-Scholes option-pricing model with the following weighted average assumptions: dividend yield of 2.6%; expected volatility of 44%; risk-free interest rate of 3.75%; and an expected life of 4 years. The weighted average fair value of each option was $3.10.

12. Countervailing and Anti-dumping Duties

On April 2, 2001, petitions for the imposition of anti-dumping and countervailing duties on softwood lumber from Canada were filed with the US Department of Commerce (DOC) and the US International Trade Commission (ITC) by certain US industry and trade groups (the Petitioners).

In response to the petitions, the ITC conducted an injury investigation and on May 16, 2002, they made a final determination that softwood lumber shipments by Canadian producers posed a threat of injury to the US softwood lumber industry. As a result of this determination, countervailing duty at 18.79% (all producers) and anti-dumping duty at 5.96% (specific to Canfor) became applicable prospectively from the date of publishing of the final order. The ITC final order was published on May 22, 2002, with the result that shipments after that date required cash deposits to be posted.

The results for the current year are after deducting $107.6 million of combined countervailing and anti-dumping duties on softwood lumber shipments to the US. While the cash payments for the anti-dumping duty are being made at the assessed rate, the anti-dumping expense has been accrued at an average rate of 5.6% for 2002, which is a best estimate of the rate applicable to Canfor's product shipment profile, as determined by applying the DOC's methodology. Canfor expects that the DOC will officially reassess the rate during their administrative review process. The difference between the assessed rate and the accrual amounted to $1.1 million in 2002, and is being carried as an account receivable in "long-term investments and other".

As a result of the ITC's ruling that Canadian lumber shipments only posed a threat of injury, in the second quarter of 2002 Canfor reversed $39.3 million of preliminary countervailing and $6.5 million of preliminary anti-dumping duties recorded in 2001.

Canfor and other Canadian forest product companies, the Federal Government and Canadian provincial governments (Canadian Interests) categorically deny the US allegations and strongly disagree with the countervailing and dumping determinations made by the ITC and DOC. Canadian Interests continue to aggressively defend the Canadian industry in this

US trade dispute and are appealing the decision of these administrative agencies to the appropriate courts, NAFTA panels and the WTO. Notwithstanding the rates established in the investigations and the posting of cash deposits, the final liability for the assessment of countervailing and anti-dumping duties will not be determined until the DOC's administrative review process is complete. An administrative review is currently expected to begin sometime after May 31, 2003 and will be completed by approximately November 2004. The completion could extend beyond 2004 with the finalization of any appeals.

13. Interest Expense

	2002			2001		
(millions of dollars)	Long-term	Short-term	Total	Long-term	Short-term	Total
Total interest cost	$ 56.3	$ 4.8	$ 61.1	$ 55.7	$ 11.6	$ 67.3
Less: Interest income	0.5	1.4	1.9	0.1	2.3	2.4
Interest capitalized	–	–	–	–	0.7	0.7
	$ 55.8	$ 3.4	$ 59.2	$ 55.6	$ 8.6	$ 64.2

14. Employee Future Benefits

Information about Canfor's defined benefit plans, in aggregate, is as follows:

	2002		2001	
(millions of dollars)	Pension Benefit Plans	Other Benefit Plans	Pension Benefit Plans	Other Benefit Plans
Plan assets, at fair market value				
Beginning of year	$ 368.9	$ –	$ 422.1	$ –
Actual loss on plan assets	(11.0)	–	(36.7)	–
Canfor contributions	2.3	2.2	1.7	1.5
Employee contributions	1.2	–	1.2	–
Benefit payments	(19.5)	(2.2)	(19.4)	(1.5)
End of year *	$ 341.9	$ –	$ 368.9	$ –
Pension and other retirement benefit provisions				
Beginning of year	$ 318.1	$ 56.8	$ 297.7	$ 43.4
Interest cost	22.8	4.1	21.6	3.1
Current service cost – Canfor	10.2	1.3	9.7	1.2
Current service cost – employees	1.2	–	1.2	–
Benefit payments	(19.5)	(2.2)	(19.4)	(1.5)
Actuarial loss (gain)	(18.2)	15.2	1.9	10.6
Plan amendments	0.3	–	5.4	–
End of year	$ 314.9	$ 75.2	$ 318.1	$ 56.8
Plan surplus (deficit)	$ 27.0	$ (75.2)	$ 50.8	$ (56.8)
Surplus (deficit)				
Plan surplus (deficit)	$ 27.0	$ (75.2)	$ 50.8	$ (56.8)
Employer contributions after measurement date	5.2	–	0.5	–
Unamortized transitional amount	(39.1)	25.7	(42.8)	27.7
Unamortized past service costs	5.0	–	5.1	–
Unamortized net actuarial loss	70.5	25.4	51.5	10.6
	68.6	(24.1)	65.1	(18.5)
Post-employment provision recognized in the Consolidated Balance Sheet (Note 9)	(2.0)	(24.1)	(4.5)	(18.5)
Prepaid pension benefits (Note 5)	$ 70.6	$ –	$ 69.6	$ –

* Canfor has adopted a measurement date of September 30 for accounting purposes. At December 31, 2002, the market value of the plan assets had increased by $11.0 million.

Included in the above pension and other retirement benefit provisions and fair value of plan assets at year-end are the following amounts in respect of plans that are not fully funded:

	2002		2001	
(millions of dollars)	Pension Benefit Plans	Other Benefit Plans	Pension Benefit Plans	Other Benefit Plans
Fair value of plan assets	$ 54.0	$ –	$ 25.0	$ –
Pension and other retirement benefit provisions	(76.9)	(75.2)	(40.2)	(56.8)
Plan deficit	$ (22.9)	$ (75.2)	$ (15.2)	$ (56.8)

Canfor's expense (income) for company-sponsored benefit plans is:

	2002		2001	
(millions of dollars)	Pension Benefit Plans	Other Benefit Plans	Pension Benefit Plans	Other Benefit Plans
Interest cost	$ 22.8	$ 4.1	$ 21.6	$ 3.1
Current service cost	10.2	1.3	9.7	1.2
Expected return on plan assets	(27.7)	–	(31.9)	–
Amortization of transitional amount	(3.7)	2.0	(3.7)	2.0
Other	1.6	0.3	0.1	–
Expense (income) recognized in the current year	$ 3.2	$ 7.7	$ (4.2)	$ 6.3

In addition to the above, Canfor's contributions to forest industry-union defined benefit pension plans amounted to $17.6 million in 2002 (2001 – $16.6 million).

Canfor also provides pension bridge benefits to certain eligible former employees. At December 31, 2002, the actuarially determined obligation for these benefits was $9.7 million (2001 – $5.2 million). The accrued benefit liability for these benefits, included in "other long-term liabilities" on the balance sheet at December 31, 2002, was $5.5 million (2001 - $5.4 million) and the related expense recognized in the current year was $1.1 million (2001 – $0.4 million).

The actuarial assumptions used in measuring Canfor's benefit plan provisions are as follows:

	2002		2001	
(weighted-average assumption as of December 31)	Pension Benefit Plans	Other Benefit Plans	Pension Benefit Plans	Other Benefit Plans
Discount rate	7.25%	7.25%	7.25%	7.25%
Rate of compensation increase	2% for 5 years 3% thereafter	n/a	3% for 5 years 5% thereafter	n/a
Expected long-term rate of return on plan assets	7.20%	n/a	7.70%	n/a

For measurement purposes, an annual rate of increase in the per capita cost of covered health care benefits of 5.3% was assumed for 2002. The rate was assumed to decrease annually to 4.2% by 2008 and remain at that level thereafter.

The above assumptions reflect management's best estimates, and are based on past experience and current economic expectations. The actual expense that will be recorded in future years is sensitive to changes in these assumptions. Based on a sensitivity analysis of a range of possible changes in the assumptions (i.e. a 0.5% change in the long-term rate of return and a 1.0% change in the rate of compensation increase), the estimated pension expense for the following year would not be materially different.

15. Income Taxes

The tax effects of the significant components of temporary differences that give rise to future income tax assets and liabilities are as follows:

(millions of dollars)	2002 Current	2002 Long-term	2001 Current	2001 Long-term
Future income tax assets				
Capital loss carry forward	$ –	$ 22.1	$ –	$ 25.3
Accruals not currently deductible	24.9	21.2	12.7	32.9
Post-employment benefits	–	11.6	–	10.4
Loss carry forward arising from restructuring of Howe Sound Pulp and Paper Limited (Note 19)	–	184.8	–	185.2
Other	0.5	6.0	0.5	1.9
	$ 25.4	$ 245.7	$ 13.2	$ 255.7
Future income tax liabilities				
Property, plant, equipment and timber	$ –	$ (371.9)	$ –	$ (376.0)
Deferred pension costs	–	(26.0)	–	(25.4)
Other	–	(2.3)	–	(1.3)
	$ –	$ (400.2)	$ –	$ (402.7)
Future income taxes, net	$ 25.4	$ (154.5)	$ 13.2	$ (147.0)

The components of income tax recovery (expense) are as follows:

(millions of dollars)	2002	2001
Current	$ (9.2)	$ (14.5)
Future*	12.7	34.0
Affiliates	(1.9)	(0.7)
	$ 1.6	$ 18.8

* On July 30, 2001, the Government of the Province of British Columbia introduced legislation to decrease the provincial general corporate income tax rate from 16.5% to 13.5%, effective January 1, 2002. As required by the Canadian Institute of Chartered Accountants, Canfor applied the rate reduction, as of its substantive enactment date, to all temporary differences that were expected to reverse after January 1, 2002. This had the effect of reducing Canfor's net future income tax liability and expense for 2001 by $18.7 million.

The reconciliation of income taxes calculated at the statutory rate to the actual income tax provision is as follows:

(millions of dollars)	2002	2001
Net income before income taxes:	$ 9.9	$ 7.6
Income tax expense at statutory tax rate	$ (3.6)	$ (3.0)
Large corporation tax	(5.2)	(4.2)
Change in general corporate income tax rate	–	18.7
Howe Sound Pulp and Paper Limited Partnership losses (Note 19)	8.0	6.3
Amounts not deductible for tax purposes and other tax adjustments	2.4	1.0
Income tax recovery	$ 1.6	$ 18.8

16. Related Party Transactions

Transactions with related parties occur at fair market value, unless otherwise noted below.

Canfor markets the pulp production of Howe Sound Pulp and Paper Limited Partnership (Note 19) for which it received commissions totaling $2.7 million in 2002 (2001 – $3.0 million) under the terms of its agency sales agreement. Canfor provides management, fibre supply and other services to Howe Sound Pulp and Paper Limited Partnership at cost, for which it received $2.2 million in fees for 2002 (2001 – $2.0 million). Canfor sells logs to Howe Sound Pulp and Paper Limited Partnership, which amounted to $8.9 million in 2002 (2001 – $13.6 million). Canfor also sold sodium chlorate to Howe Sound Pulp and Paper Limited Partnership in 2002 in the amount of $6.4 million (2001 – $5.6 million).

Canfor purchases pulp chips and lumber from Lakeland Mills Ltd. and The Pas Lumber Company Ltd. During 2002, Canfor purchased $11.5 million in pulp chips and $8.8 million in lumber (2001 – $13.5 million and $9.0 million respectively).

During 2002, Kyahwood Forest Products Ltd. provided remanufacturing services to Canfor in the amount of $6.3 million (2001 - $3.2 million).

17. Unusual Items

(millions of dollars)	2002	2001
Insurance claim	$ –	$ 8.5

18. Financial Instruments

a. Currency Risk

Forward Exchange Contracts

A significant portion of Canfor's income from operations is generated from sales denominated in US dollars. In order to manage some of the risk associated with fluctuating exchange rates, Canfor enters into forward exchange contracts from time to time. At December 31, 2002, Canfor had forward exchange contracts outstanding of US $140.0 million in total (2001 – nil). These contracts were fixed at rates ranging from $1.5817 to $1.6168 and have option periods that are spread evenly throughout 2003. As at December 31, 2002, there was an unrecognized gain on the contracts in the amount of $1.6 million.

Currency Swaps

In 2001, Canfor had US $125.0 million of cross currency swaps, which effectively fixed, at an exchange rate of $1.4035, the amount of Canadian dollars required to repay its US dollar term loan of that amount. The swaps were terminated during 2001 and a gain of $18.8 million was realized and applied against the deferred charge for foreign exchange on the outstanding term debt. This amount will be recognized into income when the related debt repayments are made.

b. Credit Risk

Canfor does not have a significant concentration of credit risk as no one individual customer accounts for 10% or more of total company sales. Canfor reviews the credit history of all new customers before extending credit and also performs regular reviews of the credit performance of existing customers. Canfor may require payment guarantees, such as letters of credit, or obtains credit insurance coverage. The allowance for doubtful accounts as at December 31, 2002 was $0.6 million (2001 – $1.4 million).

19. Howe Sound Pulp and Paper Limited Partnership

On March 10, 2001, Canfor and Oji Paper Co., Ltd. (Oji), its 50% co-venturer in the Howe Sound Pulp and Paper Limited (Howe Sound) joint venture, transferred the business of Howe Sound into a limited partnership, Howe Sound Pulp and Paper Limited Partnership (the Partnership). The Partnership continues to be jointly owned by Canfor and Oji and continues to carry on the existing operations of Howe Sound.

As part of the reorganization, Howe Sound was amalgamated with Canadian Forest Products Ltd. (CFP), Canfor's principal operating subsidiary, and, with ongoing operations of the Partnership, approximately $643.0 million of tax losses of Howe Sound are available to reduce the future taxable income of CFP. In 2001, as part of the reorganization, CFP made a payment of $60.2 million to the Partnership, which was applied to reduce the long-term debt of Howe Sound assumed by the Partnership. During 2002, additional payments totaling $5.0 million were made to the Partnership. CFP has agreed to make further payments to the Partnership, up to a maximum of $57.1 million, contingent upon its ability to utilize the tax losses of Howe Sound and payable upon utilization of the losses. These future payments will be recognized as a future income tax asset.

As a result of this reorganization, CFP recorded a future income tax asset and a deferred credit, which were $184.8 million and $95.7 million, respectively, at December 31, 2002 ($185.2 million and $104.0 million at December 31, 2001). The deferred credit will be recognized into income on a systematic basis.

Canfor wrote off its investment in the joint venture in 1998 and no longer reflects its share of the joint venture's results in its earnings. Canfor's method of accounting for its interest in the Partnership did not change as a result of the reorganization.

While Canfor does not reflect the Partnership's results in its earnings, it is required to include its share of the limited partner's income or loss, within the limits imposed by the Income Tax Act (Canada), in the calculation of taxable income. This had the effect of increasing Canfor's future income tax recovery in 2002 by $8.0 million (2001 – $6.3 million). Any income tax expense incurred by Canfor will be reimbursed by the Partnership.

The following financial information for 2002 reflects 100% of the Partnership's operations for their year ended January 3, 2003. The comparative figures reflect 100% of the joint venture's operations from January 1, 2001 to March 9, 2001 and 100% of the Partnership's operations from March 10, 2001 to its year-ended January 3, 2002.

a. Statement of Net Income of Howe Sound Pulp and Paper Limited Partnership

(millions of dollars)	January 3, 2003	January 3, 2002
Net sales	$ 338.1	$ 368.6
Costs and expense	377.3	391.9
Operating loss	(39.2)	(23.3)
Interest expense and foreign exchange loss	(8.0)	(32.0)
Loss before income taxes	(47.2)	(55.3)
Income tax expense	–	(0.5)
Net loss	$ (47.2)	$ (55.8)

b. Statement of Financial Position of Howe Sound Pulp and Paper Limited Partnership

(millions of dollars)	January 3, 2003	January 3, 2002
Assets		
Current assets	$ 97.8	$ 122.9
Fixed assets	879.5	922.4
Other assets	77.8	78.1
	$ 1,055.1	$ 1,123.4
Liabilities*		
Current liabilities	$ 109.9	$ 92.8
Long-term debt	495.2	538.6
Other liabilities	4.9	3.0
Equity	445.1	489.0
	$ 1,055.1	$ 1,123.4

* The liabilities of Howe Sound Pulp and Paper Limited Partnership are non-recourse to Canfor.

c. Statement of Changes in Cash Position of Howe Sound Pulp and Paper Limited Partnership

(millions of dollars)	January 3, 2003	January 3, 2002
Operating		
Net loss	$ (47.2)	$ (55.8)
Adjustments for non-cash items:		
Amortization	45.8	45.9
Other operating items	33.3	44.2
	31.9	34.3
Financing		
Repayment of long-term debt	(36.7)	(132.7)
Partner's capital additions	5.0	60.2
	(31.7)	(72.5)
Investing	(2.1)	(13.5)
Increase (decrease) in net cash for year	$ (1.9)	$ (51.7)

20. Earnings Per Share

Basic earnings per share are based on the weighted average number of common shares outstanding during the period. Diluted earnings per share are based on the weighted average number of common shares, convertible subordinated debentures and stock options outstanding at the beginning of or granted during the period.

(millions of dollars, except for number of shares and per share amounts)	2002	2001
Basic Earnings		
Net income	$ 11.5	$ 26.4
Less interest on equity component of convertible subordinated debentures, net of income taxes	(5.6)	(4.8)
Income available to common shareholders	5.9	21.6
Diluted Earnings		
Add back interest on equity and liability components of convertible subordinated debentures	– (a)	– (a)
Income available to common shareholders	$ 5.9	$ 21.6
Weighted average number of common shares	81,144,842	81,088,847
Incremental shares from stock options	175,265	166,756
Shares issuable upon conversion of convertible subordinated debentures	– (b)	– (b)
Diluted number of common shares	81,320,107	81,255,603
Basic earnings per share	$ 0.07	$ 0.27
Diluted earnings per share	$ 0.07	$ 0.27

(a) Anti-dilutive – $5.9 million (2001 – $5.4 million)
(b) Anti-dilutive – 11,742,424 shares issuable

Options to purchase 4,002,250 common shares at various prices, from $7.30 to $18.75 per share, were outstanding during 2002 (2001 – 3,287,750) but were not included in the computation of dilutive earnings per share either because the options' exercise prices were greater than the average market price of the common shares or, in the case of performance-based stock options, market value targets had not been met.

21. Change in Non-Cash Working Capital

(millions of dollars)	2002	2001
Accounts receivable	$ 22.7	$ 12.2
Inventories	(10.3)	41.9
Prepaid expenses	(0.8)	(3.5)
Accounts payable, accrued liabilities and current portion of deferred reforestation	58.9	(69.6)
Income taxes	2.7	3.0
	$ 73.2	$ (16.0)

22. Commitments and Contingencies

a. Operating Leases

The future minimum lease payments under operating leases are as follows:

(millions of dollars)	
2003	$ 23.6
2004	17.4
2005	11.2
2006	6.8
2007	5.0
Thereafter	15.3
Total minimum lease payments	$ 79.3

b. Canfor's investment in Lakeland Mills Ltd. and The Pas Lumber Company Ltd. is pledged as security for the bank debt of those mills.

c. As at December 31, 2002, Canfor had no commitments to purchase capital assets (2001 – $10.7 million).

d. Contingent Liability
Canfor has received a Notice of Assessment from the Income Taxation Branch of the British Columbia Ministry of Provincial Revenue with respect to property transfer taxes associated with the amalgamation of Canadian Forest Products Ltd. (CFP) and Howe Sound Pulp and Paper Limited in 2001. The notice denied CFP's claim for an exemption from property transfer tax resulting from the amalgamation of CFP and Howe Sound Pulp and Paper Limited. The potential liability arising from this assessment, including accrued interest to December 31, 2002, is $10.4 million.

In the opinion of management and counsel, the amalgamation qualifies for exemption from property transfer taxes and, therefore, CFP will vigorously contest the assessment. A Notice of Objection has been filed and no provision has been made for the amount in the accounts. As required by the Ministry, CFP has posted a Letter of Credit for the assessed amount plus accrued interest.

23. Termination Benefits and Mill Closure Costs

In October 2002, Canfor announced plans to implement a cost reduction and margin improvement program with a target to achieve $150 million in annualized benefits by the end of 2003. The specific details of the plan were approved by management in December 2002. As part of the program, a reduction to the employee base of approximately 300 people was announced and, consequently, $25.8 million of termination benefits have been accrued at December 31, 2002. An additional provision of $7.3 million has been made for costs associated with the closure of the Upper Fraser Sawmill, which will occur in the third quarter of 2003. The closure costs will include asset write-downs, demolition costs, environmental clean-up costs and other post-closure costs.

24. Comparative Figures

Certain 2001 figures have been reclassified to conform to the current year's presentation.

Subsidiary Companies

(wholly owned)

Operating Companies

Canadian Forest Products Ltd.

Canfor Europe

Canfor Panel and Fibre Marketing Ltd.

Canfor Pulp and Paper Marketing Ltd.

Canfor U.S.A. Corporation

Canfor Wood Products Marketing Ltd.

Genus Resource Management Technologies Inc.

Howe Sound Transportation Company Limited

Nanika Timber Limited

Inactive/Holding Companies

317231 British Columbia Ltd.

615157 B.C. Ltd.

B.C. Chemicals Ltd.

Canfor Hong Kong Corporation

Canfor Japan Corporation

Canfor Limited

Eburne Sawmills Limited

Northwood Properties Limited

Willowcale Storage Inc.

Joint Ventures

(proportionately consolidated)

Canfor Georgia-Pacific Japan Corporation (50% interest)

Partnerships

Howe Sound Pulp and Paper Limited Partnership (49.99% interest) (Note 17)

HSPP General Partner Ltd. (50% interest)

Investments

(equity accounted)

Kyahwood Forest Products

Lakeland Mills Ltd.

The Pas Lumber Company Ltd.

Vernon Seed Orchard Co.

Canfor Corporation – 2002 Selected Quarterly Financial Information

	1st Qtr	2nd Qtr	3rd Qtr	4th Qtr	Year ended Dec 31, 2002
		(unaudited)			(audited)
Sales and income (millions of dollars)					
Net sales	$ 505.9	$ 577.0	$ 548.9	$ 480.5	$ 2,112.3
Manufacturing and product costs	433.5	490.0	502.3	464.0	1,889.8
Amortization	29.7	27.6	28.2	29.6	115.1
Selling and administration	13.8	18.9	16.0	16.3	65.0
Reversal of duties accrued in prior year	–	(45.8)	–	–	(45.8)
Termination benefits and mill closure costs	–	–	–	33.1	33.1
Operating income (loss)	28.9	86.3	2.4	(62.5)	55.1
Equity income (loss) of affiliated companies	(0.1)	4.7	–	0.4	5.0
Interest expense	(15.4)	(14.5)	(14.6)	(14.7)	(59.2)
Other income (expense)	(0.8)	10.8	(0.5)	(0.5)	9.0
Income (loss) before income taxes	12.6	87.3	(12.7)	(77.3)	9.9
Income tax recovery (expense)	(1.5)	(17.1)	0.9	19.3	1.6
Net income (loss)	$ 11.1	$ 70.2	$ (11.8)	$ (58.0)	$ 11.5
Per common share (dollars)					
Basic	$ 0.12	$ 0.85	$ (0.16)	$ (0.73)	$ 0.07
Diluted	0.12	0.75	(0.16)	(0.73)	0.07
Cash generated from (used in) (millions of dollars)					
Operating activities	$ (9.3)	$ 85.7	$ 49.8	$ 18.2	$ 144.4
Financing activities					
Long-term debt	–	(49.9)	–	–	(49.9)
Dividends paid	(5.3)	(5.3)	(5.2)	(5.3)	(21.1)
Other	0.5	(2.7)	(0.1)	(3.0)	(5.3)
	(4.8)	(57.9)	(5.3)	(8.3)	(76.3)
Investing activities					
Property, plant, equipment and timber	(8.1)	11.9	(18.5)	(32.1)	(46.8)
Mortgage receivable on sale of property	–	(20.7)	5.0	–	(15.7)
Other	(4.2)	(5.5)	(3.7)	0.5	(12.9)
	(12.3)	(14.3)	(17.2)	(31.6)	(75.4)
Increase (decrease) in net cash	$ (26.4)	$ 13.5	$ 27.3	$ (21.7)	$ (7.3)
Summary of consolidated shipments (unaudited)					
Logs – 000 m³	184.7	362.1	369.2	312.9	1,228.9
Lumber – MMfbm					
Canfor produced	664.3	744.4	718.1	690.5	2,817.3
Purchased from other wholesale producers	53.6	67.6	89.8	66.8	277.8
Total Lumber	717.9	812.0	807.9	757.3	3,095.1
Plywood – 000 Msf 3/8" basis	41.6	41.3	42.0	37.1	162.0
Pulp – 000 mt					
Canfor produced					
Pulp segment	200.4	234.5	197.4	203.2	835.5
Pulp and Specialty Kraft Paper segment	36.5	39.9	41.1	40.5	158.0
Marketed on behalf of HSLP*	82.2	99.3	85.8	76.2	343.5
Total Pulp	319.1	373.7	324.3	319.9	1,337.0
Kraft paper – 000 mt	25.8	25.9	28.5	28.7	108.9

Certain previously published figures have been reclassified to conform to the current presentation.
* Howe Sound Pulp and Paper Limited Partnership, herein referred to as HSLP.

Canfor Corporation – 2001 Selected Quarterly Financial Information

	1st Qtr	2nd Qtr	3rd Qtr	4th Qtr	Year ended Dec 31, 2001
		(unaudited)			(audited)
Sales and income (millions of dollars)					
Net sales	$ 481.6	$ 511.2	$ 535.3	$ 457.6	$ 1,985.7
Manufacturing and product costs	403.3	436.3	474.6	443.4	1,757.6
Amortization	27.5	26.6	26.1	25.8	106.0
Selling and administration	14.5	17.3	14.9	12.9	59.6
Operating income (loss)	36.3	31.0	19.7	(24.5)	62.5
Equity income (loss) of affiliated companies	(1.0)	1.3	1.4	(0.6)	1.1
Interest expense	(15.6)	(16.9)	(17.0)	(14.7)	(64.2)
Other income (expense)	0.8	(0.1)	(0.6)	(0.4)	(0.3)
Unusual items	8.5	–	–	–	8.5
Income (loss) before income taxes	29.0	15.3	3.5	(40.2)	7.6
Income tax recovery (expense)	(10.2)	(5.2)	16.1	18.1	18.8
Net income (loss)	$ 18.8	$ 10.1	$ 19.6	$ (22.1)	$ 26.4
Per common share (dollars)					
Basic	$ 0.22	$ 0.11	$ 0.23	$ (0.29)	$ 0.27
Diluted	0.21	0.11	0.21	(0.29)	0.27
Cash generated from (used in) (millions of dollars)					
Operating activities	$ (59.2)	$ 56.9	$ 54.4	$ 66.7	$ 118.8
Financing activities					
Long-term debt	116.1	(50.1)	–	–	66.0
Dividends paid	(5.3)	(5.2)	(5.3)	(5.3)	(21.1)
Other	(0.3)	(3.3)	1.4	14.0	11.8
	110.5	(58.6)	(3.9)	8.7	56.7
Investing activities					
Property, plant, equipment and timber	(7.2)	(16.0)	(10.2)	(17.8)	(51.2)
Other	(60.2)	(14.0)	(0.4)	4.1	(70.5)
	(67.4)	(30.0)	(10.6)	(13.7)	(121.7)
Increase (decrease) in net cash	$ (16.1)	$ (31.7)	$ 39.9	$ 61.7	$ 53.8
Summary of consolidated shipments (unaudited)					
Logs – 000 m^3	301.6	302.4	369.3	267.5	1,240.8
Lumber – MMfbm					
Canfor produced	512.9	547.7	603.7	601.6	2,265.9
Purchased from other wholesale producers	72.6	64.8	68.7	67.7	273.8
Total Lumber	585.5	612.5	672.4	669.3	2,539.7
Plywood – 000 Msf 3/8" basis	37.4	44.5	39.6	40.1	161.6
Pulp – 000 mt					
Canfor produced					
Pulp segment	184.9	212.4	199.0	195.7	792.0
Pulp and Specialty Kraft Paper segment	31.3	35.9	39.3	41.6	148.1
Marketed on behalf of HSLP*	71.9	101.9	83.8	80.9	338.5
Total Pulp	288.1	350.2	322.1	318.2	1,278.6
Kraft paper – 000 mt	24.6	26.4	28.3	27.4	106.7

Certain previously published figures have been reclassified to conform to the current presentation.
* Howe Sound Pulp and Paper Limited Partnership, herein referred to as HSLP.

Canfor Corporation – 5-Year Comparative Review

	2002	2001	2000	1999	1998
Sales and income (millions of dollars)					
Net sales	**$ 2,112.3**	$ 1,985.7	$ 2,265.9	$ 1,741.2	$ 1,424.7
Manufacturing and product costs	**1,889.8**	1,757.6	1,822.1	1,414.3	1,260.1
Amortization	**115.1**	106.0	112.7	70.2	65.2
Selling and administration	**65.0**	59.6	67.5	47.9	59.6
Reversal of duties accrued in prior year	**(45.8)**	–	–	–	–
Termination benefits and mill closure costs	**33.1**	–	–	–	–
Operating income	**55.1**	62.5	263.6	208.8	39.8
Equity income (loss) of affiliated companies	**5.0**	1.1	1.2	7.8	(5.6)
Interest expense	**(59.2)**	(64.2)	(60.4)	(33.2)	(38.0)
Other income (expense)	**9.0**	(0.3)	7.5	(0.5)	1.4
Unusual items	**–**	8.5	(2.5)	–	(38.0)
Income (loss) from continuing operations before income taxes	**9.9**	7.6	209.4	182.9	(40.4)
Income tax recovery (expense)	**1.6**	18.8	(83.8)	(76.0)	12.4
Income (loss) from continuing operations before losses related to Howe Sound	**11.5**	26.4	125.6	106.9	(28.0)
Discontinued operations	**–**	–	–	(4.3)	(3.8)
Loss from and write-off of investment in Howe Sound, net of taxes	**–**	–	–	–	(171.9)
Net income (loss)	**$ 11.5**	$ 26.4	$ 125.6	$ 102.6	$ (203.7)
Per common share (dollars)					
Before discontinued operations and losses related to Howe Sound	**$ 0.07**	$ 0.27	$ 1.50	$ 1.75	$ (0.48)
Basic	**0.07**	0.27	1.50	1.68	(3.49)
Diluted	**0.07**	0.27	1.36	1.66	(3.49)
Dividends paid on common shares	**0.26**	0.26	0.26	–	0.065
Book value per share	**10.27**	10.35	10.24	9.72	7.30
Assets and capitalization (millions of dollars)					
Working capital	**$ 273.2**	$ 344.4	$ 71.1	$ (15.2)	$ 261.0
Long-term investments	**94.7**	71.3	74.0	69.8	62.2
Property, plant, equipment and timber	**1,424.2**	1,469.0	1,518.4	1,384.8	610.4
Other assets and deferred charges	**139.3**	159.9	116.8	93.1	99.3
Net assets	**$ 1,931.4**	$ 2,044.6	$ 1,780.3	$ 1,532.5	$ 1,032.9
Long-term debt	**$ 643.4**	$ 714.7	$ 400.9	$ 442.1	$ 473.0
Other accruals and provisions	**83.9**	118.4	64.8	49.6	37.7
Future income taxes	**154.5**	147.0	363.9	139.0	96.2
Deferred credit	**95.7**	104.0	–	–	–
Common shareholders' equity	**953.9**	960.5	950.7	901.8	426.0
Total capitalization	**$ 1,931.4**	$ 2,044.6	$ 1,780.3	$ 1,532.5	$ 1,032.9
Additions to property, plant, equipment and timber (millions of dollars)	**$ 68.5**	$ 54.7	$ 121.8	$ 119.9	$ 40.8

	2002	2001	2000	1999	1998
Cash generated from (used in) (million of dollars)					
Operating activities [(a)]	$ **144.4**	$ 118.8	$ 99.8	$ 225.3	$ 83.3
Financing activities					
Long-term debt	**(49.9)**	66.0	(50.2)	19.5	(12.2)
Common shares	**–**	–	0.1	239.5	–
Dividends paid	**(21.1)**	(21.1)	(21.1)	–	(3.8)
Interest on convertible subordinated debentures, net of income tax	**(5.5)**	(4.3)	(4.7)	–	–
Other	**0.2**	16.1	(0.7)	–	–
	(76.3)	56.7	(76.6)	259.0	(16.0)
Investing activities					
Property, plant, equipment and timber	**(46.8)**	(51.2)	(110.8)	(119.9)	(40.8)
Howe Sound Pulp and Paper Limited Partnership	**(5.0)**	(60.2)	–	–	–
Investment in subsidiaries and affiliates	**–**	–	–	(433.2)	–
Mortgage receivable on sale of property	**(15.7)**	–	–	–	–
Other	**(7.9)**	(10.3)	(8.6)	13.5	8.4
	(75.4)	(121.7)	(119.4)	(539.6)	(32.4)
Increase (decrease) in net cash					
From continuing operations [(a)]	**(7.3)**	53.8	(96.2)	(55.3)	34.9
From discontinued operations	**–**	–	–	13.8	3.9
	$ **(7.3)**	$ 53.8	$ (96.2)	$ (41.5)	$ 38.8
Financial statistics					
EBITDA	**170.2**	168.5	376.3	279.0	105.0
Return on capital employed	**2.7%**	3.5%	9.3%	12.3%	(10.9)%
Return on common shareholders' equity	**1.2%**	2.8%	13.6%	15.4%	(38.5)%
Ratio of current assets to current liabilities [(b)]	**1.7:1**	2.0:1	1.1:1	1.0:1	1.7:1
Ratio of net debt to shareholders' equity [(a), (b)]	**41:59**	43:57	42:58	41:59	48:52
Production statistics					
Pulp – 000 mt	**1,001.5**	900.1	980.1	521.8	453.2
Kraft paper – 000 mt	**107.6**	108.8	109.9	103.7	104.6
Lumber – MMfbm	**2,960.1**	2,260.3	2,235.3	1,423.8	1,378.3
Plywood – 000 Msf 3/8" basis	**165.4**	168.7	158.7	–	–
Hardboard – 000 Msf 3/8" basis	**26.3**	24.8	24.1	22.9	23.8
Refined fibre – 000 mt	**39.5**	40.2	38.5	33.9	29.4
Sales by product line					
Log sales	**6%**	6%	7%	10%	9%
Pulp and kraft paper	**30**	34	39	26	26
Lumber – Canfor produced	**52**	48	41	42	46
Lumber – Other producers	**6**	6	8	17	14
Plywood	**3**	3	2	–	–
Miscellaneous	**3**	3	3	5	5
	100%	100%	100%	100%	100%
Sales by market					
Canada	**20%**	21%	20%	22%	21%
United States	**57**	55	54	56	58
Europe	**10**	11	15	10	11
Far East	**12**	12	10	11	9
Other	**1**	1	1	1	1
	100%	100%	100%	100%	100%

(a) Certain prior years' figures have been reclassified to conform to the 2002 presentation.
(b) For 1998 and prior years, ratios have been restated to exclude the assets, liabilities and debt of Howe Sound Pulp and Paper Limited.

Directors and Officers

Directors

The names, principal occupations, municipalities of residence, and the periods during which they have been Directors of the Company are as below. For more information visit www.canfor.com.

P.J.G. Bentley, O.C., LL.D. (1)(4)(5)
Chairman of the Board,
Canfor Corporation
Vancouver, British Columbia
Director since 1966

R.L. Cliff, C.M., F.C.A. (1)(2)(3)(4)
Chairman of the Board,
Heathcliff Properties Ltd.
West Vancouver, British Columbia
Director since 1983

M.L. Cullen (2)(3)
Corporate Director,
Surrey, British Columbia
Director since 2000

C.W. Daniel, O.C., LL.D (3)(5)
Corporate Director;
Consultant
Toronto, Ontario
Director since 1985

D.L. Emerson (1)
President and Chief Executive Officer,
Canfor Corporation
Vancouver, British Columbia
Director since 1998

M.E. Hurst (4)(5)
Educational Author
Vancouver, British Columbia
Director since 1987

J.B. Jarvis (1)(2)
Corporate Director
Vancouver, British Columbia
Director since 1966

P.A. Lusztig (2)(4)(5)
Dean Emeritus,
University of British Columbia;
Commissioner (Federal),
B.C. Treaty Commission
Vancouver, British Columbia
Director since 1983

E.P. Newell, O.C. (3)(4)
Chairman and Chief Executive Officer,
Syncrude Canada Inc.
Fort McMurray, Alberta
Director since 1999

M.E.J. Phelps, O.C. (1)(3)(4)
Chairman, Dornoch Capital Inc.
West Vancouver, British Columbia
Director since 1990

R.T. Riley (4)(5)
Vice-President of L.B.G.
Capital, a Division
of National Bank Financial
Montreal, Quebec
Director since 1987

C. Taylor, O.C. (5)
Chair of the Canadian
Broadcasting Corporation
Vancouver, British Columbia
Director since 2000

Officers

The names, offices held, and municipalities of residence of the officers of the Company and the offices held by them are as below. For more information visit www.canfor.com.

P.J.G. Bentley, O.C., LL.D.
Chairman
Vancouver, British Columbia

D.L. Emerson
President and Chief Executive Officer
Vancouver, British Columbia

C.W. Reid
Group Vice-President,
Finance and Chief Financial Officer
Surrey, British Columbia

J.B. Engleson
Group Vice-President, Wood Products
Prince George, British Columbia

B.R. Hislop
Group Vice-President and
Chief Technology Officer,
Vancouver, British Columbia

R.A. Luoma
Group Vice-President, Pulp and Paper
Prince George, British Columbia

J.R. Williams
Group Vice-President, Fibre Management
Surrey, British Columbia

K.O. Higginbotham
Vice-President, Forestry and Environment
Surrey, British Columbia

J.K. Pau
Vice-President and Treasurer
Vancouver, British Columbia

R.L. Waldie
Vice-President, Human Resources
Prince George, British Columbia

S. Yurkovich
Vice-President, Corporate Affairs
Vancouver, British Columbia

D.M. Calabrigo
General Counsel and Corporate Secretary
Surrey, British Columbia

K.J. Clayton
Corporate Controller
North Vancouver, British Columbia

(1) Member of the Executive Committee, which acts generally on behalf of the Board of Directors between meetings.

(2) Member of the Audit Committee, which reviews the Company's financial statements, the scope and results of the external auditor's work, the adequacy of internal accounting and audit programs and compliance with accounting and reporting standards.

(3) Member of the Management Resources and Compensation Committee, which makes recommendations to the Board regarding the Company's pension plans and the remuneration of its Directors and senior officers and ensures management development and succession programs are in place.

(4) Member of the Corporate Governance Committee, which ensures that the Company through its Board of Directors sustains an effective approach to corporate governance.

(5) Member of the Environmental, Health and Safety Committee, which develops, reviews and makes recommendations on matters related to the Company's environmental, health and safety policies, and monitors compliance with those policies and with government regulations.

The term of office of each Director expires on the date of the next Annual General Meeting of the Company.

Canfor Operations

	Lumber (Mfbm)	2002 Production	2003 Capacity [5]
	Primary Mills		
1	Chetwynd	218,400	226,500
2	Clear Lake	145,600	175,400
3	Fort St. James	264,800	290,900
4	Fort St. John	201,000	290,000
5	Grande Prairie	207,700	212,800
6	Hines Creek	94,700	95,000
7	Houston	451,700	445,000
8	Isle Pierre	238,300	245,000
9	Prince George	229,800	359,200
10	Polar	245,000	265,000
9	Rustad	289,400	290,000
11	Taylor	75,000	60,300 [6]
12	Upper Fraser	303,100	213,600 [7]
	Sub-total	**2,968,500**	**3,168,700**
	Remanufacturing		
	Canfor USA[1]	141,100	160,000
2	Clear Lake	31,000	39,400
5	Grande Prairie	7,600	17,000
9	PG Wood Treating Plant	5,100	7,000
13	Kyahwood[3][4]	25,000	28,200
	Sub-total	209,800	251,600
	Total Lumber	**3,178,300**	**3,420,300**
	Plywood (Msf)		
9	North Central Plywood	**165,400**	**174,300**
	Pulp (mt)		
9	Prince George Pulp and Paper	158,400	141,800
9	Intercontinental	304,700	307,000
9	Northwood	538,400	551,900
14	Howe Sound[3]	342,900	348,600
	Total Pulp	**1,344,400**	**1,349,300**
	Paper (mt)		
9	Prince George Pulp and Paper	**107,600**	**134,600**
	Newsprint (mt)		
14	Howe Sound[3]	**206,100**	**208,200**

(1) not shown
(2) jointly owned with Riverside Forest Products, Weldwood of Canada and West Fraser Timber
(3) includes 100 per cent of production
(4) 50 per cent joint venture
(5) assumes full annualized production from capital projects in Fort St. John and Prince George sawmills. 2003 production is expected to be 2,944,500 mfbm
(6) sawmill line to close 3rd Quarter 2003
(7) to close 3rd Quarter 2003

Other Operations

15 Corporate Office
15 Canfor Wood Products Marketing (Toronto, ON office not shown)
15 Canfor Pulp and Paper Marketing
Canfor Georgia-Pacific Japan Corporation[1]
Canfor Europe[1]
15 Canfor Research and Development Centre
9 BC Chemicals
16 Englewood
9 Executive Office
9 Administration Centre
17 Harrison
15 Panel and Fibre

Nurseries/Seed Orchards

9 J.D. Little Forest Centre
5 Grande Prairie
18 Sunshine Coast
19 Vernon Seed Orchard[2]

Woodlands

Prince George Operations
Fort St. James Operations
Houston Woodlands Operations
Alberta-Peace Operations
Coastal Operations

Corporate and Shareholder Information

Annual General Meeting
Canfor's Annual General Meeting will be held at the Four Seasons Hotel, Le Pavillon Room, 791 West Georgia , Vancouver, B.C., on Tuesday, April 29, 2003 at 11:30 a.m.

Transfer Agent and Registrar
CIBC Mellon Trust Company
Vancouver, Calgary, Regina, Winnipeg, Toronto, Montreal and Halifax

Stock Listing
Toronto Stock Exchange
Symbol: CFP

Investor Contact
Charles W. Reid
Group Vice-President, Finance and Chief Financial Officer
Telephone: (604) 661-5200
Fax: (604) 661-5484

Auditors
PricewaterhouseCoopers
Vancouver, B.C.

Canfor Corporation
Head Office
#1500 – 550 Burrard Street
Vancouver, BC
V6C 2C1

Telephone: (604) 661-5241
Fax: (604) 661-5235
E-mail: info@canfor.ca
Web: www.canfor.com

Canfor also produces an Annual Information Form. To obtain this publication or more information about the company, please contact Canfor Corporation, Corporate Affairs.

Lee Coonfer
Manager, Corporate Communications
Telephone: (604) 661-5225
Fax: (604) 661-5219

CANFOR

www.canfor.com